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# MARKETING
## ITS PROBLEMS AND METHODS

BY

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# PREFACE

This book has been written to meet the need in schools and colleges for a text covering the general methods and problems of marketing raw materials, farm products and manufactured goods. A broad survey of these methods and problems is a necessary foundation for more specialized studies, for the same reason that a broad survey of economic principles should precede courses in banking, transportation, or labor problems.

Raw materials and farm products form the best means of studying marketing methods functionally. The distributive machinery for handling them is not only more complex than that for manufactured goods, but the activities are also more highly specialized, and the functions more clearly defined. For this reason, the discussion in Part I deals with the marketing of these commodities from a functional point of view.

The marketing of manufactured products presents a series of problems so complex, so distinct in character, and yet so immediate and practical in every way, that it may be studied by the "problem method." It is for this reason that Part II treats the marketing of finished products largely by means of a progressive series of problems.

In this way variety is secured without losing sight of the fact that the entire economic process is a more or less continuous one. Influences affecting the marketing of raw materials and farm products are often reflected in the marketing of finished goods. The reverse is also true. The method of presentation in this discussion takes due cognizance of this fact.

There is to be found in this book something more than a mere description of the existing distributive organization. The analysis goes deeper than this, and isolates and defines causes and influences. It aims in a real sense to be a book of "applied" economics. The historical background is given whenever needed for an understanding of problems or functions, but history and description are alike secondary considerations. Illustrations are here in abundance to furnish evidence and to make the discussion concrete. It may be said that the primary purpose is by means of a descriptive analysis to translate facts into principles.

Most of the material for this book has been accumulated through years of teaching classes in marketing, and of investigating practical problems. The method of approach has thus been thoroughly tested, both from a pedagogical and from a practical point of view. In general outline, the method is very simple, consisting of three essential parts: (1) analysis of the commodity, (2) the analysis of the market, and (3) the analysis of the trade organization. It has the two merits of simplicity and unassailable logic. The writer believes that he has been able to put the content of fact into the outline and has given significance to this analysis.

The writer has drawn material from various publications. Acknowledgment of this fact has been made at the appropriate places. Suggestions for the underlying analysis will be found in a series of lectures given years ago by Mr. MacMartin at the University of Minnesota. It was inevitable that as a teacher, the writer should have profited by the work of his students, and for this invaluable aid he desires to give due credit. For criticism and helpfulness in many ways the writer is indebted to his wife, Beatrice S. Duncan. For making the index he is under obligation to Margaret S. Merwin.

C. S. DUNCAN

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# MARKETING
# ITS PROBLEMS AND METHODS

## CHAPTER I

### INTRODUCTION

**1. Definition.**—Commercial organization is to be distinguished from both business organization and industrial organization. Business organization is the general term for the entire economic system of production and distribution; it is correlative with the term profession or diplomacy, just as one speaks of the professional man, the business man, or the diplomatist. Of this general term commercial organization is a part, but a part only. From industrial organization it differs in that it has to do with the actual distribution of goods, the buying and selling process, while industrial organization deals with the manufacturing process. The terms most nearly synonymous with commercial organization are marketing and merchandising. Marketing, however, has local and provincial meanings, illustrated by "to go marketing," "to do the marketing," that mar its effectiveness for the more general meaning. Merchandising is being specialized to indicate the bargaining process between buyer and seller, and is becoming synonymous with salesmanship. Commercial organization as used here, then, means the mechanisms and devices in modern industrial society for the actual transfer of economic goods, whether by wholesale or retail, from one party to another, on their way from origin to consumption. A study of commercial organization is, therefore, a study of marketing problems and methods.

In the discussion of economic theory, commercial organization becomes a part of distribution, but overlaps into production. From a broad point of view, there are but two parts of the economic process; one is production, the other, consumption. If the creation of value is the essence of production, then the distributive process, since it does add value to economic goods, is a part of production. The best means of keeping the meaning clear is to think of economic goods moving from their source to the doors of the factory, or to the consumer, and from the doors of the factory to consumer, through the mechanism of commercial organization. It includes all of the processes of transportation, storing, weighing, grading, buying, selling, etc. Commercial organization has to do primarily with the activities of the merchant; industrial organization has to do primarily with the activities of the manufacturer.

**2. Place of Commercial Organization in the Economic Process.**—All economic goods move in a more or less continuous process from origin to consumer. Some steps of the process are often simultaneous, as, for instance, when goods are bought and sold in transit or during manufacture, or when the merchant stores his consignments of goods at the beginning of a season. There is no absolutely clear-cut line of demarcation between industrial and commercial organization. Industrial and commercial problems are, therefore, interlacing. The manufacturer, in locating his plant, will have to consider the problem of transportation, of buying his raw materials, and of selling his product. These are commercial problems. The merchant will need to consider the location of his store or warehouse, the construction and equipment of his plant, the processing or routing of his goods, and the management of his labor force. These problems are usually treated as production problems.

The general relationship of commercial activities to the other economic activities may be visualized by means of the following diagrammatic sketch:

| I | II | III | IV | V | |
|---|---|---|---|---|---|
| Raw Materials | Extractive Industries | Commercial Organization | Manufacturing Industries | Commercial Organization | Consumer Demand |
| Transportation | | | | | |
| Financing | | | | | |

It will be seen by this diagram that commercial organization always stands between the goods and the market. The extractive industries may be farming, mining, forestry, or fishing. If the products, thus derived, are not for direct consumption, if they are to go to the market, or if they are to be bought and sold, then commercial problems arise. The manufacturer must buy his materials or reach back to their source and control the intervening commercial process himself. And when the same manufacturer, with his materials fabricated, looks out toward his market, he faces once more the need of commercial organization and commercial problems.

In fact, commercial problems are the most fundamental of all business problems. The *alpha* and the *omega* of the business process is merchandising, buying and selling. The manufacturer, as well as the merchant, has his purchasing department and his sales department. He buys his raw materials; he sells his finished product. The beginning of every business process is buying; the end of every business process is selling, or consumption. The problem of demand is a commercial problem; the problem of supply is a commercial problem. These statements hold true for abstract economic goods, like services, as well as for concrete economic goods, like shoes.

Furthermore, it will be observed from the above diagram that some economic activities are pervasive. The problem of transportation is not confined to the merchant or the manufacturer. It is a part of the entire economic process. Why are railroads called public utilities, *i.e.*, private property devoted to public service? Because transportation is a necessary, fundamental activity to the entire business organization. What affects it, affects the welfare of all men; it is, in fact, a public service. In the same way, financing is a pervasive process, and the welfare of all men is involved. Hence, the special laws to regulate banks. Possibly insurance, as it is developing in these latter days, will have to be added to this list.

This discussion shows in a general way where commercial organization belongs in the course of business activity. It stands between the manufacturer and his supply of raw materials; it stands between him and the market for his finished goods. The same principle holds where the raw materials of one manufacturer are the finished products of another, as for instance, pig iron, or steel ingots, or steel plates, or the entire list of semi-manufactured goods. It holds true also of that vast volume of foodstuffs which do not pass through the process of fabrication on their way to the consumer.

**3. Relation of Commercial Organization to Commercial Geography.**—The beginning of wisdom in a study of commercial organization is a knowledge of natural resources. That is to say, a prerequisite for a discussion of commercial problems is a course in commercial geography. The whole framework of trade has shaped itself to meet the difficulties and to make the most of the advantages of every geographic region. It is always modified by historical considerations and by tradition, but in the slow process of time it adjusts itself to facilitate in the best possible way the distribution of economic goods. The trade problems of the United States rest upon the physical basis of natural resources and commercial organization has adjusted itself to the physiographic helps and obstacles to the flow of trade. These problems of trade cannot be intelligently discussed except in connection with the location of mineral and ore deposits, coal beds, oil basins, and great trade centers; the courses of important streams, especially the navigable ones; the network of railways; the coastwise and lake trade routes; the corn and cotton belts; the wheat growing regions; the grazing ranges; and the general population movements.

It is necessary to have a panoramic view of the economic situation as a preliminary to a detailed discussion of individual problems. Such a bird's-eye view can best be had through a study of geography, in both its commercial and its industrial aspects. Our new interest in foreign trade has revealed an appalling ignorance of geography, even among those who have transacted business beyond the borders of our country. A much denser ignorance probably prevails among those who have not given attention to questions beyond their immediate business affairs in local markets. The interlocking character of modern business demands a broader outlook for the future. Commercial organization, as discussed here, assumes a good general knowledge of commercial geography.

**4. Study of Commercial Organization More than a Study of Merchandising.**—A study of the problems of commerce is more than a study of the art, or science, of buying and selling; that is, of merchandising, in the sense of making a bargain, of "putting through a deal," of "higgling in the market." Its scope is much broader, and, in a true sense, more fundamental. The act of buying or of selling advantageously is the consummation devoutly to be wished; it is the culmination of a process. This is a matter of human contact, and it is shot through and through with psychological problems. A most important step it is, but nevertheless only a part of the journey.

No broad, sound business policy can be developed from a study merely of this merchandising function. A far broader basis than shrewd bargaining is needed for really good business. No lawyer would dare to enter the court room with a knowledge only of the case in hand, however thorough that knowledge might be. Rather has he studied this case, not only in itself, but also as related to many other cases, to decisions of other analogous cases, and particularly in relation to the principles of law involved. The physician follows the same mental processes. A patient is in part an individual problem; in a broader sense all patients fall into groups and certain principles apply to each group; but scientific treatment goes beyond these matters of human contact to the more profound and fundamental things of diagnosis and scientific principles involved.

In a similar way, the business man should analyze his problems. It is a narrow, shortsighted policy to concentrate on the mere act of buying and selling. This method leads to get-rich-quick practices. It is not a way to build up a permanent, respectable business, whose foundations are laid broad and deep on a well-considered, broadly-planned, and thoroughly-analyzed policy. The professional business man needs to study the entire background of his business; he needs to know where he belongs in the scheme of things; how he is situated relatively to the present flow of trade; and what the tendencies of trade are that affect him. To do this he must look beyond the higgling and bargaining process. He must study not only the art and science of buying and selling, but also the whole mechanism of trade organization.

**5. Functions and Institutions.**—With the growing complexity of industry and commerce, there has been a tendency more and more to isolate certain economic services, or functions. This process is one of specialization. Formerly, in simpler times, a business man combined the capacities of manufacturer, financier, carrier, warehouseman, wholesaler, retailer, and risk taker. A widened market, a greater volume of trade, a more speculative business make such a simple situation no longer possible. There have developed what are known as functionalized middlemen, or those men, such as railroadmen, insurance men, wholesalers, retailers, bankers, who devote their effort to a specialized phase of business activity.

Because these functions belong to all business activity, because they are an essential part of the distributive mechanism as it now exists, they are called systems, such as the credit system, the banking system, the transportation system, the warehouse system. This means that these services are an organized part of the distribution of economic goods.

There are, then, those economic activities for certain well-defined economic ends that are called functions. One may speak of the functions of the wholesaler, of the retailer, of the credit manager. The functions of the wholesaler are to collect goods in relatively small quantities from a great variety of sources, the process of concentration, to sort, grade, and combine them in lots demanded by jobbers and retailers, to distribute to these jobbers and retailers at the time and in the quantity desired by them, and to finance the transaction as far as necessary. As an organized function of the entire distributive system wholesaling may be called an institution.

**6. Institutional and Functional Analysis.**—The above distinction is insisted upon not alone for the sake of clear thinking but also to point out that commercial problems may be analyzed from either one of these points of view. One may study the banking system as an institution, guided by its own principles, revolving on its own axis. In the same way, one may treat the credit system as an institution, or the railroads, or the warehouses, or retail stores or exchanges, and so on. Or one may discuss the commercial problems on a functional basis, and isolate the functions of middlemen.

It will be found, however, that functions cannot be separated from institutions, and institutions, in whatever sense used, cannot be intelligently discussed apart from functions. In fact, they are not things apart from one another. Institutions are organized for the purpose of facilitating the performance of certain functions. The character of the service determines the type and character of the institution. The service, or function, is, therefore, more fundamental.

**7. Commodity Analysis.**—It is possible also to analyze commercial problems from the point of view of a given commodity. Thus, one may trace the course of cotton, or wheat, or corn, or cattle, or steel, or leather, or any other commodity bought and sold on the market, from its source to the consumer, and study the commercial problems connected with it. This will give a specialized knowledge that is invaluable so far as the specific commodity is concerned. Such an analysis will not, however, demonstrate broad principles. From such a basis of knowledge, one cannot know for himself why there is an organized exchange for cotton and wheat and not for wool; he cannot know whether staple goods can be advertised as well as style goods. One may know thoroughly that one subject, but he cannot generalize from it. A single commodity is only an illustration, and it may be a pertinent and vivid one, too, but it will not establish a principle. On the other hand, if one commodity after another is taken up in succession, there will necessarily be duplication.

The conclusion becomes inevitable. The best method of analyzing the commercial problems is by a combination of the three methods suggested. Institutions and functions may be studied through illustrations. That is the logical, scientific method. It is the method to be followed in this discussion.

**8. Types of Economic Goods.**—No one has yet made a searching analysis of the types of economic goods as they flow through the market. There is possible at this time, therefore, only a general grouping, with broad twilight zones to separate them. This broad classification will serve as a working basis, however, until a more nearly scientific study is made. In this discussion, goods "on the market" will fall into one or the other of two general groups; one is called raw materials and foodstuffs, the other is manufactured products. The full justification for this division will appear as the discussion develops. A practical justification may be stated here. The great bulk of raw materials and foodstuffs come through to the factory or the consumer with little or no intervention of the manufacturer—unless, of course, the original producer is so called. With the development of the canning and preserving industries, even this distinction is disappearing. In the second group, the manufactured products, it is obviously intended that the manufacturing process shall be predominant.

**9. Raw Materials and Foodstuffs.**—As has been said the great bulk of raw materials and foodstuffs reach the fabricating plant or the consumer without any intervening manufacturing process. They thus arrive at their market essentially in their natural state. Some manufacturing, some production always takes place, of course, since coal and ore must be broken to convenient size and timber must be cut or even sawn into lumber, and fish, fowl, and meat animals may be killed and cleaned. In spite of these qualifications, the vast bulk of such commodities come to market practically in their natural state.

From this fact two or three important consequences follow. In the first place, these commodities are formed by the forces of nature and not by man. They do not come into being in accordance with a predetermined plan that man has made. Wheat and corn do not grow to match the changes in fashion; ore was formed wholly independent of style. These things must be taken as they are produced by the laws of nature, and, if necessary, adapted to the wants of man. Since these commodities are produced by forces beyond the control of man, it follows also that they do not readily fall into any standard patterns. Standards are difficult to apply to them.

Another point to be considered is that within this group fall the materials essential to the very existence of man. For these essential materials the demand is established. It is the supply that is to be regulated, and for a control of which there is a never-ending struggle. In fact, one of the most vital things to watch in studying the marketing problems connected with this group of commodities is the control. And since many of them are perishable, there is a large speculative element and consequent risk. The two important things to watch in the marketing of raw materials and foodstuffs are control and risk. As these goods are on their way through the trade organization, who has the control, who bears the risk?

**10. Manufactured Goods.**—The distinguishing characteristic of this group is the obvious one, namely, that the fabricating process is of paramount importance in preparing materials for human consumption. It is at this point that machinery has entered most conspicuously, with its attendant problems. For commercial analysis the particular point to be considered in this connection is the development of the repetitive process, with its accompanying standardization and setting of fixed patterns.

Manufacturered goods, in form and texture, are controlled by the will of man. He transfers his will, along with his thought, skill, and intelligence, to his machines. Fabrication is just this process of molding, modifying, shaping the crude materials in accordance with the manufacturer's will. But the manufacturer is only in very small part the originator of the form and texture of his products. He takes his orders from the market; he adapts his production to the consumer's demand. And just here arise the forces to make the marketing problems of finished products distinct from those of raw materials and foodstuffs. For out of this power of control grows the power to identify, to brand, to trade-mark goods. Here enters also that most powerful force, advertising. And so, whereas in the marketing of raw materials and foodstuffs emphasis is to be placed upon the control of the commodity and the risk of its destruction or deterioration, in this case the emphasis is upon the control of consumer's demand. An entire series of different problems arises from this distinction.

**11. Business Facts and Business Principles.**—There is a persistent fallacy among business men that the problems of each individual business are unique. In a superficial sense all problems are unique, just as no two leaves are exactly alike. Similarly, examples in arithmetic, problems in algebra, theorems in geometry are unique. But there are mathematical principles underlying them all, and there are business principles common to all business problems, "if men would but with patience distil them out."

"Herein may be illustrated the dividing line between the general principle and the unique problem of each business. The law, the rule, the principle is general, the facts are unique, are individual. It is, of course, the most difficult problem of all to see the general rule behind the unique facts."[1]

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[1] Duncan, *Commercial Research,* p. 347.

Hard-headed business men who would not for a moment believe that one swallow makes a spring, seem prone to accept one instance as demonstrating a business principle. Business writing is full of arguments from a single instance to a general law. There have not yet been collected and analyzed enough business data from which to develop scientific rules; the very best that can be done is to be careful and comprehensive. One great value of a general discussion of this kind lies in guiding the reader by a descriptive analysis into careful methods of business research.

**12. Commercial Problems and Business Research.**—The great body of available business facts is yet to be organized and analyzed. Scientific principles have only very recently been applied to them. The general business man has never had the training or the leisure time to do research work. Here the field is all ready for the harvest.

It is one primary purpose of this discussion to point the way to a careful analysis of business problems. While there will be given here a descriptive analysis of the general framework of trade organization for handling both manufactured and unmanufactured goods, the real benefit to be derived from a study of the trade organization is to carry some given commodity along through that study. It is, therefore, energetically urged that some such supplementary work be done.

The analysis of commercial problems may be made analogous to experiments in physics and chemistry, although the scientific precision of the latter is not possible in the former. A business laboratory is at hand in every trade center; the principles of business are operating everywhere. The business facts, from which business principles are drawn, are not to-day in books; they are on the street, in the shop. Commercial problems are not static, but dynamic. They shift and change from day to day. Hence their great difficulty and hence also their perennial interest.

Their complexity and their difficulty afford a stimulating intellectual challenge.

**13. Commercial Problems and Statistics.**—One cannot go far in a study of commercial problems without finding need for at least an elementary knowledge of statistical methods. The student of business problems will be in almost constant contact with figures. These will be thrown at him in all sorts of odd forms, sometimes distorted to produce a certain effect, sometimes unwittingly twisted awry, sometimes bungled by crude but fallacious methods of classification. One should know how to hold his mental equilibrium under all circumstances. He must be able to bring order out of chaos, to identify error, to present clearly and effectively the truth. To be able to do this, he must have a workable knowledge of statistical principles.

**14. Commercial Problems and Economic Theory.**—A knowledge of the general principles of economics is assumed in this discussion. As a matter of fact, it is necessary here to apply those general principles. There are courses in engineering schools called applied mechanics and applied mathematics. So this study might be called one in applied economics. The law of diminishing returns, or of marginal utility, or of supply and demand, is not merely a thing in a book, but a live, actuating principle of business life. The factors of production may be seen at work in all trade centers. When this fact is realized, there is no longer any thought of economics as a "dismal science"; it becomes surcharged with life; it is fascinating, absorbing.

**15. Commercial Problems and Business Management.**—There is frequent mention in these days of business becoming a profession, and the business man a professional man. Before this condition can be realized, business men must have professional training. By professional training is meant the securing of a practical familiarity with an organized body of principles which are to be applied to certain types of problems. This is true of training in the medical profession, in the legal profession, in engineering, in all professional schools. If the practitioner or judge be transformed into a business manager, one finds an analogous case. For the business manager to become professional, he must master the body of principles in accordance with which his problems are resolved.

Business capacity is, after all, only the ability to solve correctly as they arise the business problems that confront one in carrying on an enterprise. Commercial problems come before the business manager daily. If he is not to solve them in a hit-or-miss fashion, if he is to discard his rule-of-thumb methods, he must acquaint himself with such principles as are illustrated in this discussion.

**16. History of Commerce.**—He will be best prepared to take up a study of the current commercial problems who has been well grounded in the historical development of commerce. Most problems have an important and instructive ancestry, and tradition is a powerful, conservative force in all kinds of business. Change is the haunting fear of most business men.

A survey of the industrial and commercial history of the United States, at least, should precede a course on marketing. American business institutions are only British business institutions transplanted to a new country, fabulously rich in natural resources, and institutions that have been modified and improved and sometimes transformed by the shrewdness, skill, and daring of American business men. The greater the knowledge of the industrial and commercial history of Great Britain, the better equipped one is to understand our own problems.

**17. Commercial Law.**—Business is transacted under legal restrictions. Many business problems pivot on legal issues. A striking example is found in competition itself. What is unfair competition? The answer is for the courts to make, and they will make it from legal precedents and business facts. Private property and contract are fundamentally legal questions. Obviously, therefore, some knowledge of commercial law is necessary for an intelligent discussion of business problems.

**18. Educational Value of Commercial Study.**—Within recent years there has been a rapidly growing appeal for the study of present-day business problems. In general, education has been turning to a study of life as it is, rather than to study life as it was or is thought to have been. If life is to be lived intelligently in the midst of the vast problems that surround us, it behooves one to focus his attention on them. It is for this reason that a study of business is coming to be looked upon as having cultural value. A careful scrutiny of business problems does not need to make one materialistic. The large part of human relationships are business relationships. Why, therefore, should they not receive the serious attention of thoughtful men?

## Suggestions for Study

The following points will afford the basis for a discussion preliminary to an analysis of marketing problems:

### I

1. Origin of commercial organization.
2. Historical development of commercial organization.
3. Functional analysis of commercial problems.
4. Modern tendencies in commercial development.
5. Machine industry and trade organization.
6. Specialization in trade organization.
7. Business integration and trade organization.
8. Relation of government to trade organization.

Readings:

Commons, *Labor Administration,* pp. 219-264.

Duncan, *Commercial Research,* Chap. XI.
Nystrom, *Economics of Retailing,* Chap. II.
Shaw, *Some Problems of Market Distribution,* pp. 7-23.
Smith, *Industrial and Commercial Geography,* pp. 675-683.
Weld, *American Economic Review,* June, 1917, pp. 306-318; August, 1917, pp. 565-575.

## II

1. Economic research versus scientific research.
2. Economic laws in business.
3. Obstacles in the way of accuracy in business research.
4. Sources of business facts.
5. Analyzing business facts.
6. Interpreting business facts.
7. Business facts and business policies.
8. Business research and competition.
9. Research and commercial education.
10. Governmental responsibility for commercial research.

READINGS:

Calkins, *Business of Advertising,* Chap. V.
Casson, *Ads. and Sales,* Chap. III.
Cherington, *Advertising as a Business Force,* Chap. I.
Copeland, *Business Statistics,* pp. 207 et seq.
Duncan, *Commercial Research,* Chaps. III, IV, X.
French, *Advertising,* Chap. XII.
Lewis, E. St. E., *Industrial Management,* series of articles, October, 1916, to February, 1917, pp. 10, 225, 289, 684.
Martin, S. O., "A Scientific Study of Marketing." *Annals of the American Academy of Political and Social Science,* May, 1915.
Parlin, *Printers' Ink,* February 10, 1917.

## III

1. The problem of reducing business experience to figures.
2. The value of the proper unit.
3. Eliminating the bias.
4. The "personal equation" in business statistics.

5. Are statistical methods scientific?
6. The question of business barometers.
7. The practical use of the "mode."
8. The construction and significance of index numbers.
9. The problem of proper weighting.
10. "Inertia of large numbers."

READINGS:

Babson, *Business Barometers for Forecasting Conditions,* Chaps. I, IV.
Brookmire, *American Economic Review,* vol. iii, pp. 43-58.
Copeland, *Business Statistics,* pp. 3-97.
Duncan, *Commercial Research,* Chap. IX.
Persons, *American Economic Review,* December, 1916, pp. 736-769.
*The Annalist,* September 10, 1917, p. 331.

It is suggested that each student should select at once some commodity to be studied. The best method is to follow the line of personal interest, and a study should be planned to carry through both the raw-material and the finished-product stage. An analysis of the commercial problems should be persistently followed until some considerable mastery of them is obtained. It has been frequently verified by experience that interest increases with increased knowledge. No commodity is so prosaic or so commonplace as not to yield an abundant harvest of interesting facts and experiences.

The selection of a commodity is an important step and should be taken only after consideration. The particular points to be considered are, (*a*) personal interest, (*b*) material, (*c*) possibility of seeing actual marketing process, (*d*) connection with future plans.

Immediately upon selecting the commodity the student should set about working up a bibliography. The points indicated above for study and discussion may well occupy the class-room discussion while the student is preparing the bibliography.

If the course is to bring the best results in training, it is absolutely necessary to insist from the start upon thoughtful, careful, and neat work. The bibliography, for instance, should be made on cards, with accurate references, and arranged topically to cover the following chapters in the discussion of raw materials and foodstuffs. In preparing the reports on each problem, careful references should be made to all authorities. Habits of good, businesslike workmanship may thus be established.

# PART I

# RAW MATERIALS AND FOODSTUFFS

# CHAPTER II

## ANALYSIS OF THE COMMODITY

**19. Purpose.**—In the study of practical business affairs the economic world is found to be a going concern. Economic goods are flowing onward day and night from their source to the consumer. It is a complex, intricate, closely related mechanism that is to be studied, and no single phase can be wholly isolated from its setting and analyzed as a thing apart. Commodities are drawn to market by the force of human wants, and on their way the original materials are modified in response to the requirements of that demand.

There is, then, an interaction between a commodity and the demand for it; they are complements. And these two, the commodity and the demand for it, react upon each other through a series of intermediaries known as middlemen. Strictly speaking, therefore, a commodity may be studied completely in its commercial relationship only in connection with the distributive system and the consumer demand. For the purpose of a careful and comprehensive analysis, however, the problem may be broken up into constituent problems. It is proposed here to sketch the analysis of a commodity, as an article of merchandise, as marketable goods. This analysis can be applied to any kind of a commodity, whether a material thing or a service.

**20. Method.**—The study will be carried forward under two general headings: (1) the characteristics of the commodity and (2) the supply of the commodity. Under the first topic the commodity is considered more or less philosophically, by abstracting it and thinking about it in its various commercial aspects. It is an analysis from a qualitative point of view. Under the second topic the commodity is studied quantitatively. The queries that arise are: Where found? How produced? How much? How prepared? and so forth.

**21. Characteristics of the Commodity.**—A commodity, to be marketable, must be adapted to satisfy some human want. If nature does not prepare it so that it may be directly used, some sort of preliminary process is necessary. This is a commercial consideration. So, wheat must be threshed; meat must be dressed and packed; fruit must be picked; coal must be mined; tea must be cured. In general, some sort of productive process is needed. But apart from these productive considerations there are many qualities, of commercial significance, to be examined. Just as the Interstate Commerce Commission has endeavored to examine all classes of commodities that enter into traffic on the basis of their characteristics that affect transportation, so commodities for the market must be analyzed for all of their characteristics that affect their marketing.

**22. New or Established Commodity.**—One of the first queries that arise is whether or not the commodity is a new one on the market or a long-established one. There may be a well-worn path to market, with traditional methods of preparing and handling, or there may be the problem of educating the consumer in new tastes. Oranges and lemons are found to-day even in the remotest hamlet; they may be said to be thoroughly established. And yet there are men and women still living who remember the days when they were not. The grape fruit is a later development, is less widely and thoroughly established. Casaba melons are still newer. Peanuts are comparatively recent on the market. Word was returned from Europe that some peoples there nearing starvation still looked upon canned corn as fit only for animal food.

Many of the minerals have been known for a very long time, although new uses have from time to time been developed. Iron is to-day considered the "barometer of trade." Copper, lead, zinc, silver, gold, mineral oils are established. Of recent date, however, are monazite sand used for incandescent gas-light mantles, manganese for high-speed steel, cryolite for preparing aluminum, asbestos that is entering into so many familiar, every-day things, and even phosphate rock and nitrates for fertilizer. The list of commodities could be almost indefinitely lengthened by the enumeration of by-products, such as bone dust, cotton seed, slag, etc., of new products to satisfy established wants, and of long-known commodities to meet new wants.

In raw materials and foodstuffs of all kinds, it is necessary to inquire into their status. If these materials go into an established commodity, or if as foodstuff they are directly applied to satisfy an elemental want, the commercial problems are different from those connected with an innovation. In the former case attention is focused on methods of preparation, or production, and distribution; in the latter case the problem pivots on the development of the want.

**23. Necessity or Luxury.**—A second practical inquiry is whether or not the commodity may be classed as a necessity or as a luxury. A thin line divides between these two categories, but the distinction is a practical one. Iron may be called an industrial necessity; so likewise with coal and copper. Sugar and milk are a dietary necessity to-day, if the standard of living is maintained. That commodity may be called a necessary of life which is essential to the general maintenance of the existing standard of living. If this commodity for any reason fails, then a satisfactory substitute must be had or the standard of living falls. Thus, phosphates and nitrates are necessary to maintain the productive quality of the soil. If these cannot be had from phosphate rock or nitrate of soda, then other sources must be tapped or production falls. The same principle holds for human beings. Certain elements are required for food, for clothing, for shelter, in order to maintain the existing economic well being. These are necessaries. All things beyond, however commendable and to be desired, are luxuries.

Goods pass from the one group into the other; luxuries develop into necessities. This is economic progress. Salt has from time immemorial been a necessity, while grapefruit, alligator pears, and the whole list of exotic fancy groceries are not. In raw materials and foodstuffs, therefore, there are necessities and luxuries.

As will appear more concretely later on, this is a practical distinction. It is obvious, however, that the control of one kind of material would differ in effect from the control of another. It is clear, also, that necessities are pulled by an irresistible demand into the market, while luxuries must be pushed upon the market. In one case, too, the question of price is more important than in the other. The customer of the fancy grocery makes price a secondary or incidental consideration. The dependableness of the demand, the freedom from whimsicality, freakishness, and caprice are characteristic of the demand for the necessities.

**24. Staple or Novelty.**—Very closely connected with the preceding consideration is the classification of the commodity as a staple or a novelty. In general, all necessities are staples; all luxuries are novelties. The distinction turns, however, not so much on whether or not the commodity is long established among human wants as on whether or not there is an element of style connected with it. As far as raw materials are concerned, the effect is indirect, being reflected back from the finished product. Among foodstuffs the "fancy" types are novelties. Apples may be bought by the barrel—common apples, good, ripe, juicy. But apples may also be bought wrapped up in tissue paper, particularly large, fine specimens, or a "hot-house" variety. Strawberries in wintertime may be novelties; whereas in the early summer at the height of the season they are staples. Milk of good quality may be delivered at the back door every morning in the year. But one may also buy, at probably twice the price, a "certified" quality. The former is a staple; the latter a novelty. Sugar may be only "plain" sugar, or it may be "loaf," "tea," "powdered," or other "fancy" kinds.

A staple is a commodity in general use, a common item in industry or human dietary. It is purchased for its native inherent qualities. A novelty is a commodity of special qualities. The purchaser pays for more than the native qualities—either special care in selection, in handling, in packing, or some other attempt to give distinction to it. But the distinction is almost wholly relative. What is considered a staple by one individual or group may be considered a novelty by another individual or group. It is a matter of personal taste, of purchasing power, of standard of living. There is the fancy grocery group just as there is a silk stocking group.

**25. Perishable, Semi-perishable, Non-perishable.**—It is necessary commercially to note the perishability of a commodity. The dominating factor in marketing milk or ripe fruits is their perishability. A whole series of special problems arise from this fact. Many commodities have been considered non-perishable when in reality this was not the case. Farmers have stacked their hay in the fields and left it to withstand the elements as best it might. Cotton growers have been careless in exposing cotton to the weather. In the West and in Argentina wheat is left in the field after threshing. These and countless other careless methods have caused a great social waste.

Not only are there the gross errors of leaving corn to rot in the fields, letting coal slake in the rain and snow, permitting weevils to invade the grain bins, but there is also the nice problem of bringing the perishable product to market in proper condition. The banana, a perishable product, must be carried thousands of miles to market. Strawberries, grown in the South, are to be served on the tables of New England. Oysters are delivered fresh over a wide area. Special means to make these things possible have been devised. But first a study had to be made of when to pick, how to pack, what the temperature necessary to bring them to market in proper condition.

**26. Dependability of Supply of Commodity.**—There may or may not be a steady flow of the commodity. The amount may be practically controllable, as is true of all natural resources which are still abundantly available. Coal and ore and stone and salt, and timber perhaps, can be adjusted to market demand as it manifests itself. It is merely a question of preparing an output program. The situation becomes much more complex where the supply is uncertain and its location is not certainly known. It is estimated that all of the gold and silver produced in modern times would not pay common wages to those who have prospected and dug for them. It is said, too, that the output of petroleum has never paid back what has been spent in drilling for it.

Crops are always exposed to the whims of the weather. Their output cannot be accurately predicted even up to the time of harvest. To forecast the quality is still more difficult. In the last weeks of its maturity rust may attack the wheat, or the rye, or the oats. A drought may shrivel the corn in full tassel. A week of rain may rot the potatoes. A storm may beat off the fruit.

Many products, too, are seasonal. It requires a year to grow a new cotton crop. Three or four years are necessary to bring beef cattle to marketing maturity. Two years at least are needed for sheep. Hogs mature more quickly, but no appreciable change can be made in the supply in less than six months. Oranges or lemons may require five or six years; coffee seven or more; rubber a much longer period.

Important commercial problems arise from these facts. The supply for the coming period of six, twelve, or more months, or for years can be pretty definitely charted when the returns are all in at the close of the season. The cotton crop is fairly well defined by November 1; the wheat crop is known a little earlier; corn about the same time. The "visible supply" then approaches the total supply.

Much depends, also, upon market conditions at planting, sowing, and breeding time. At this time the producers estimate what it will be profitable for them to do, whether to increase or decrease acreage, to sell the stock or retain the cattle, sheep, and hogs for breeding purposes. When these decisions are made the lines begin to form that will determine the coming season's supply.

There are many modifications here, however. The acreage of winter wheat may be determined in the autumn, but if there are clear indications before spring that this acreage is too small, or if the wheat is "winter killed," some recuperation may be had by an increased spring wheat sowing. Where the season proves bad for certain major crops, too, there may be possible some kind of "catch-up" crops to compensate in part. Another modification to be considered is the fact that the great staples have now a world-wide range. Wheat of Argentina ripens at an interval of six months from the winter wheat of the United States. Australian wheat relieves a famine in India. Thus, while within a certain political division there may be extreme fluctuations, throughout the world these can be somewhat leveled out.

A commodity, therefore, may be seasonal, intermittent, or steady in supply. Where there is uncertainty of any sort as to supply, whether because of uncontrollable natural forces or too great control through private ownership, there will be created a speculative element in the market. The great staple food crops are the most speculative commodities that enter the market.

**27. Control of Supply.**—Under our system of private property rights and national control it becomes necessary to inquire, not only into the amount possibly available, but also into the control of materials. The past few years have taught the nations of the world the "strategy of minerals."[1] This lesson came home to the United States only less keenly than to the European countries. In the competition of the future the query will be more than where the essential materials may be found; it will include also the control thereof. The United States desires to build ocean cables and finds gutta percha essential to that industry. Satisfactory supply can be had only from British territory in the Straits Settlements. Cryolite is necessary for the efficient production of aluminum, and its sole source is in Greenland mines under control of the Danish Government. Manganese is essential for high-speed steel and the Brazilian or other foreign supplies must be tapped. Quebracho wood is sought from South America for tanning; nitrate of soda from Chile for a fertilizer; asbestos from Canada or South Africa.

For a single commodity or for a whole industry certain materials may be pivotal. In such a case conditions may arise where the control of pivotal material enables an individual, a corporation, or a state to drive a hard bargain. "It is not difficult, however, to imagine conditions even in times of peace, in which it might become desirable to use the possession of these assets as an instrument of commercial negotiation."[1] It is wise to know, as far as possible, that the road to materials is assuredly an open highway.

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[1] See George Otis Smith, *The Strategy of Minerals.*

**28. Substitutes.**—The business mind revolts at control. Note the feverish search for substitutes to take the place of nitrates from Chile, for building material to take the place of the dwindling supply of timber, for the cultivation of fruits and nuts to make up for the diminishing harvest from native trees. Rubber may be now made synthetically. A manufactured combination may displace sole leather in boots and shoes.

It is part of business acumen to investigate the possibilities of substitutes for any given commodity. Here is the field for ingenuity. The world rests secure, even though it may prove to be in a fool's paradise, in the belief that something will be developed to take the place of natural resources as they are exhausted. It is a lazy attitude, and leaves a part of the commercial problem unsolved.

**29. Units of the Commodity.**—Goods are bought and sold on the basis of some kind of unit. Cotton has the bale, round or square, for its unit; coal in quantities has the ton, or in less amounts the bushel, pound, basket, or briquette; apples may be handled by the barrel, crate, pound, or individually; eggs by weight, count, dozen, or crate; hides and skins "per piece"; hay by the ton; wheat by the bushel or the quarter; oranges by the crate or dozen; tea by the pound or chest; gold or silver by the ounce or bar; milk by the bottle, quart, or pint; gas by the thousand cubic feet. Every commodity develops its unit of calculation, which becomes familiar to the trade.

Some analytical inquiry should be made into the unit of calculation. Because one exists and is familiar in the trade, is not proof that it is most convenient or most economical. It is true, however, that once established a unit is hard to eradicate. British experience is apropos here. There are units used in England that seem awkward elsewhere, but the British stubborn pertinacity retains them. A "quarter" of wheat is an example. Even a hundred-weight in England contradicts itself, being in reality one hundred and twelve pounds. The guinea is odd, too, for it is not a coin, never was a coin, and equals the curiously awkward number of twenty-one shillings.

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[1] Report of British Dominions Royal Commission, p. 163.

The point to be emphasized is that here is another phase of the analysis of a commodity to be studied. Familiarity should, of course, be had with the common units. These units should furthermore be examined critically to see if improvements may not be made. Tradition should not be permitted to keep an inconvenient and uneconomical unit fastened upon business. The simple count method in dealing with eggs is fast disappearing. A bushel of apples is now being inquired into as to quality, size, flavor. This is one way for business to progress.

**30. Requiring or Not Requiring Preparation.**—A further consideration in the analysis of a commodity is the preparation required to fit it for the market. This may be a simple or a complex process, expensive or inexpensive, technical or not. Whatever it is should be known. The curing of furs, as well as hides and skins, is most important. The pasteurizing of milk is equally so. The process of curing tea is very difficult and requires great skill. Such a commodity as crushed stone requires a distinct process of preparation for the market, so that whereas the original stone seems readily available from the fields where it lies, it is nevertheless, because of the necessary preparation, brought under the control of a business organization. There are three distinct activities in the process of preparing crushed stone for the market, the quarrying, the crushing, and the screening. Considerable capital is required in opening up a new quarry. This tends to concentrate the business in the hands of a few concerns. Here the commercial consequences are revealed.

Each commodity will have certain peculiar problems connected with its preparation for the market. A brief survey may perhaps show that salt by whatever process obtained is equally savorous, that the mining of an ore is of no material concern. It is necessary, nevertheless, to discover these facts. It is a part of the commercial problem.

**31. Independent or Group Product.**—A commodity may go independently to satisfy human wants. The demand is therefore directly for it. This is true in general of foodstuffs. Coal may pass directly to the grate, stove, or furnace to be burnt for giving warmth to human beings, or it may go into coke for use in making steel. Here the demand is for the machine and affects coal only indirectly. Cryolite, which is used in purification of aluminum, is likewise affected indirectly. Manganese, that is to be used for hardening steel, has a demand which is dependent on the demand for steel.

It is needful to keep in mind this point. The question should be asked: Does this commodity have an independent demand or an indirect or group demand? In the former case the lines run directly from the wants to the commodity; in the latter case this demand may be one, two, or more steps removed. In this latter case, too, the fate of the commodity is involved in the fate of all the others. Each in its turn may become pivotal.

**32. Varieties, Species, etc.**—A complete analysis must necessarily include a study of the varieties, types, and species of a commodity. The names given to these will usually be taken from the geographical locality, from the shape or appearance, or from certain other qualities. There are many varieties of tea but the best known are those based upon producing districts. There are the India, Chinese, Japanese, Ceylon, Java, and Formosa teas. Of salt there are two general kinds, common salt and table salt, differing only in fineness of grain and carefulness of handling. Sugar is divided into two general kinds, cane and beet, and each is subdivided into raw and refined. Refined sugar is graded as follows: granulated, powdered, confectioners', cube, and soft. Pig iron goes by the following names: Bessemer, low-phosphorus, basic, foundry, forge or mill, malleable, white, mottled or mixed, direct castings, spiegeleisen, ferro-manganese, ferro-silicon.

The varieties of a commodity may or may not be directly related to grades; they may or may not be directly related to uses. Bituminous coal has these "commercial grades": caking or coking coal, non-coking, cannel, cherry, splint, free burning, binding, block, gas, steam, etc., or steam-boat, broken, heater, egg, stove, range, chestnut, pea, buckwheat, rice. It can be seen that there is here a mixture of uses and shapes. The common varieties of peanuts are the Virginia Runner, Virginia Bunch, African or North Carolina type, Spanish type, the Valencia, or Tennessee Red type, the Georgia Red, and Red Spanish type. Distinction is made between Sea Island cotton and upland cotton. Egyptian cotton is also a distinct type.

On one basis or another certain types of a commodity become known by a name. This name may designate certain qualities or certain forms, or it may indicate only the producing region or some producer. It may be significant or insignificant commercially. But sooner or later the name will have some relation to quality and price. Expert grain inspectors can, by a mere glance, identify the producing region and each producing region is identified with certain characteristics of the grain.

**33. Physical and Chemical Tests.**—To be scientific the analysis of a commodity should extend to physical and chemical tests. One of the first tests of corn is to determine the amount of moisture it contains. Simple mechanical devices are used to sort out certain sizes of apples, oranges, or potatoes. Eggs are now consistently candled before marketing. Ores are tested chemically for their relative constituent parts. Oranges are sometimes put to chemical tests also to determine the amount of acid. Industrial chemistry for analytical purposes has become a profession. "The miller of to-day has, in his own mill, or at his easy command the laboratory equipment and the services of a skilled chemist who furnishes him accurate advance information on the new wheat he is about to handle. He knows what are its moisture per cent, gluten color, and gluten elasticity. He knows for his baker customers' direction what are its required absorption, time of fermentation, time of proofing, time of baking, etc."

An extension of such analysis means more intelligent business; it means putting business on a more scientific basis. The resulting knowledge should become available not only for the manufacturer whose demand for materials is exacting, but also for the dealer and for the general merchant. To discover such knowledge and to use it is part of the commercial problem.

Such analysis as has been suggested in the foregoing pages may be almost indefinitely extended. Along with the scientist, the business man must grow in knowledge of the physical world, and this increasing knowledge must be transmitted into business wisdom, that is, applied to business problems. The ultimate goal of all analysis of commodities is to adapt them most economically to human wants. Because business is carried on for a profit is no reason why it should be carried on crudely or ignorantly. The process of investigation may well begin with an analysis of the commodity.

**34. Supply of Commodity.**—A second general phase of the analysis of a commodity is largely statistical in character. It has to do with amounts and with values. But there are other things to be considered also. One needs to know something of the means of production, something of the geographical location of the producing regions and their delimiting characteristics. At this point commercial geography can be of much service. It is to be kept in mind throughout this section as well as the preceding one, that every item finds expression someway or other in the trade organization. In fact, one cannot justly or wisely judge the organization of trade without such information.

**35. Means of Production.**—A broad survey of the marketing problem will involve the study of the means of production. It may become a critical consideration that machinery may be applied to all important operations. The development, for instance, of a cotton-picking machine might prove revolutionary. There is one operation in handling wheat which still for the most part must be done by human hands. This is shocking the wheat in the field. In some wheat producing regions this step has been wholly eliminated. It is important to know that sugar beets and peanuts represent the ''family type'' of cultivation. This fact has affected, and may at any time again affect, the supply, through social forces wholly apart from these commodities.

The future competition in growing cotton will be greatly determined by the existence of an adequate, adaptive labor supply. Cattle hides and horse hides are by-products of cattle and horse raising. What affects the business of breeding cattle and horses will affect the supply of hides. Are the conditions changing to the detriment of cattle and horse raising? Sheep may be grown either for wool or mutton. Conditions affecting the producing of sheep may affect the supply of either or both.

Only by a careful investigation and by keeping in close touch with all changes in methods of producing a commodity can the real significance of this point be revealed. The method in vogue may be destructive of important qualities in the commodity or it may be unnecessarily expensive. The point of view of the dealer and the information which his experience may bring to the subject, will be of much help in correcting these uneconomical or wasteful practices. Dealers in eggs have already done much to improve the conditions under which they are produced. Commission merchants have helped to tone up the fruit-growing business. Cold-storage men, having learned from experience that it is all important for commodities to go into storage in first class condition, are trying to educate the producers into better methods of production. Milk dealers have been concerned in teaching milk producers the elementary principles of bacteriology, in order that production methods may be improved and a better product may be put on the market. In many cases it has been found necessary to build pasteurizing plants in the country to gain control of the milk at the earliest possible stage.

The merchant should always be interested in the methods of producing the goods he handles; the manufacturer is necessarily so. A jobber in canned goods formerly bought his products from the farmer growers when, where, and as he could. In order to gain credit for the care which he used in selecting, preserving, and canning fruits, he placed his name and trade-mark on the cans. One season he bought an unusually fine quality of peaches, which he canned and gave a special name. It sold well. But the following season he could find nothing to match them in quality or flavor. Complaints were made by the consumer that the name on the can was deceptive for it did not indicate the same quality of goods as before. In order to control the quality of fruit going into his cans, this jobber bought orchards and took care that there was proper spraying, proper picking, and proper handling of the fruit.

**36. Geographical Location of Producing Regions.**—There is not only the question of how the commodity is produced but also the question of where it is produced. This inquiry is directly concerned with the fluctuation in supply. There is, too, the most economical region of production as well as the most economical method. It is possible to-day to make a world survey of productive possibilities.

The location of natural resources has been irrevocably established by the laws of nature. Commercial and industrial organization must adjust itself to this situation. In a true sense this is a "natural monopoly." But the producing regions for commodities are often likewise limited by other requirements. The productive region for sugar beets is very narrowly limited to certain physical and climatic conditions. So far only a small area is fitted for their production. These sections appear in Michigan, Minnesota, Nebraska, Colorado, and some small parts of other western states. The producing region for tea is limited by the need for a copious water supply. It is necessary to have from 100 to 250 inches of rainfall per year. Rice has similar requirements. The producing regions for coffee, for rubber, for bananas are limited for similar reasons. The United States has its "corn belt" and its orange region. Just as minerals may be determined in location by natural laws, so the growth of vegetables is determined by soil or climatic conditions.

Even within the area available for production, there may be a contest between crops. Wheat is known as a pioneer crop and is driven onward by the advance of settlements and crops more lucrative under intensive cultivation. Peanuts demand a special kind of soil and climate and labor supply. It is said: "Wherever cotton thrives the peanut finds a home." Between these two crops there is competition. The struggle for diversified farming in the South is another type of crop competition.

Gradually crops adjust themselves to the most economical location. There are good reasons for certain counties in Wisconsin being the greatest milk-producing sections in the world. The abnormal price adjustments during the recent war, however, tended to upset this industry. A new demand or an abnormal demand may at any time disturb crop locations and affect supply. Some movement, some agitation is almost constantly causing readjustments of a more or less material character.

**37. Historical Survey of Producing Regions.**—An historical investigation should be made to ascertain whether forces are at work to increase or to decrease the productive area. In cotton new species are being experimented with. A region in the Southwest may prove to be profitable for Egyptian cotton. Within recent years the cotton-producing region has spread to new states. The cattle and sheep ranges in the West have been decreasing in area. The orange-growing area fluctuates, especially in the South, reaching farther and farther north during the years when no frost molests. Then will come a killing freeze, and the region suddenly contracts. Due to the guaranteed price for wheat, the acreage sown increased within one year by from 10 per cent to 20 per cent in certain mid-Western states. It is all important for one whose interests are affected by crop production to follow the shifting process with the movement of population. Production has its great movements of ebb and flow as well as its fluctuating waves.

Here, too, comes a study of the elasticity of supply and its reaction to changes in demand. The cattle buyers in the Chicago stock market know how long it requires a change in price to affect the oncoming supply. A series of prosperous years for growers of oranges and lemons caused the planting of new orchards to such an extent that within a space of five years the orange output was expected to double and the lemon production to increase 50 per cent. A season of glutted market may cause a half or more of the strawberry beds to be plowed up or let run wild. Two or three poor seasons for peaches have caused the cutting down of many orchards. The price of silver has reopened many an abandoned mine. All such facts are of commercial significance.

**38. Characteristics of Producing Regions.**—It is important to consider not only the location and limitation of the productive region, but also the commercial bearing of these facts. Wheat has a far-flung productive region, extending throughout different climates, the crops coming to maturity and being harvested at different seasons; the harvest season is long and the wheat flows into market for several months; there is less chance for a complete failure of crop; more varieties are possible; it is a real or potential competitor with other crops; it is adapted to large or small farms. These, among other facts of commercial significance, result. In contrast, cotton and oranges and sugar beets are grown in concentrated areas. One influence may materially affect the entire output; the whole crop is subject to the same climatic conditions; varieties are limited; the bulk comes to market at once; an increase of supply means more intensive farming; with a narrow growing region and a broad demand there tends to be a one-crop system.

Wool shows a broad producing region with certain concentrated areas. Sheep raising may be an incident to farming or it may be the dominating industry, as on the ranges. As has been said, sheep may be produced for their wool or for mutton. The supply of lumber is being more and more narrowly defined, through lack of a far-sighted foresting policy. Many industries are thus compelled to keep moving with the receding timber line. There are now clearly defined forest regions in the United States: the North-western, Central, Southern, Rocky Mountain, and Pacific regions. The content of these regions has been estimated as follows:

| FOREST REGION | Area (Million acres) | Stumpage (Billion feet) |
|---|---|---|
| Northern | 90 | 270 |
| Southern | 150 | 630 |
| Central | 130 | 300 |
| Rocky Mountain | 1,000 | 300 |
| Pacific | 80 | 1,300 |

This careful charting of supply makes possible a tight control over output. The saying that one should not keep all of one's eggs in a single basket is particularly appropriate when applied to a tropical enterprise. Only by means of a very widely scattered area of production, and a diversified list of products, is the industry of the tropics enabled to withstand the sweeping disasters that nature there is prone to hurl upon it. This broadly distributed source of supply seems as a system of self-insurance against the forces of destruction that man cannot control. A violent hurricane can, in a very few minutes, utterly destroy the banana crop of an entire island or district. But experience has shown that if one's producing regions be scattered widely enough a bumper crop in one region will at least partially compensate for the loss which hurricane, flood, or drought has inflicted in another.

The producing area of each commodity has its own peculiar problems. These can be discovered and analyzed only by a careful survey. In general, the commercial significance of each characteristic should be examined. The tendency of each area to increase or to decrease in amount, to improve in quality, to change in variety should be carefully observed.

**39. Volume of Production.**—An analysis of a commodity will include a statistical investigation of the volume of output through a sufficient number of years to demonstrate all tendencies. Variations in volume must be accounted for, in order to isolate the influences at work and to evaluate them. The period examined should cover a sufficient length of time to give the necessary background for judging the existing conditions.

**40. Value of Output.**—A further study should be made of the value or market price of the commodity. This examination will be carried on especially in its relation to the volume of output. A comparison of these two items will throw much light upon market conditions and the influences at work there.

**41. "Visible Supply."**—Wherever possible a study should be made of the surplus or "visible supply," of the commodity. This amount may be what is on record at any particular moment, in storage, on board freight cars, or on board ships. It is the amount available for trade. Of special significance, however, is the "visible supply" at the close of the season. In fact, one of the most important parts of the analysis is a comparison and an interpretation of the relation between the volume of output, the value, and the "visible supply."

**42. Conclusion.**—This survey has indicated the most important points to be kept in mind when analyzing a commodity. It has been shown that a careful, philosophical, and, if possible, scientific examination of the qualities of each product is of great commercial significance. A charting of quantity and value is likewise necessary. It must be remembered that all of these things are of importance in their bearing upon the market and the trade organization.

## SUGGESTIONS FOR STUDY

The discussion in this chapter should be applied to the commodity selected by each student for research. The following points are suggestive of work to be done:

1. Let the student supply himself with a base map of the United States, then go to one of the following sources and locate on the map the productive region for: (*a*) cotton; (*b*) wheat; (*c*) livestock; (*d*) petroleum; and other commodities.

   *References:*
   - *Statistical Abstract.*
   - *United States Atlas.*
   - Department of Commerce, Bureau of Census, Bulletins 128 (1914), 131 (1915), etc.
   - Thirteenth Census, Volumes v, vi, vii.
   - *Yearbook of the Department of Agriculture.*
   - Reports of U. S. Geological Survey.
   - Various handbooks.
2. From the same sources secure the necessary data to show:
   - (*a*) Volume of production in the United States for ten, fifteen, or twenty years.
   - (*b*) Value of annual crop for same period.
   - (*c*) Surplus or "visible supply" for same period.

   Chart these figures on the same sheet for comparison.
3. Enumerate the factors that have made for (*a*) increased production, or (*b*) decreased production.
4. Interpret your charts from the point of view of these factors, accounting in this way as fully as possible for all significant fluctuations.
5. In the light of these facts, what is the prophecy for the future?
6. Interpret the characteristics of the producing areas into commercial terms.
7. Write up the first part of your report on the commodity selected for special study. Cover all of the points brought out in this chapter.

# CHAPTER III

## ANALYSIS OF THE MARKET

**43. The Market.**—The market in its broadest sense means demand, or in economic phraseology, effective demand—a demand with the compelling force of purchasing power behind it. It is in some such sense as this that the term is used here. From the producer's point of view the market is a chance to sell. The coal-mine operators sell coal to dealers; the lumberman sells his product to the wholesale dealer, the retail dealer, the manufacturer of furniture, of wagons, of a thousand other things of which lumber is a part.

But market may also refer to the region, the commercial area within which the buyers dwell. Manufacturing establishments are concentrated in the cities; hence, the markets for the raw materials which they use are in the cities. The surplus foodstuffs from the farms move toward the centers of population; the larger the centers the greater the markets. In most cases, however, certain centers are highly specialized markets, are concentration points. Some explanation must be sought for the fact that, while the crude ore of aluminum is mined in Arkansas, the smelting center is St. Louis, and the purifying centers are in New York State, and the factories for making aluminum ware are elsewhere. For a clear understanding of the marketing of copper, reasons must be found for the fact that the bulk of the supply comes from mines in western United States, but the world price has in recent years been determined in Bremen, Germany. Why should Elgin have become the great market for butter?

Commercial demand is oblivious of both national and state boundaries. If such a demand were charted, political lines would be crossed and recrossed. One investigator has claimed that a careful survey would discover a *sauerkraut* territory, a right-hand plow territory, a wide-wheeled wagon region, and so on. These commercial areas would run riotously across state lines, county lines, and physical boundaries. And yet there must be somewhere some clear and reasonable explanation for such things.

Every analysis, of course, runs back at last to the elemental fact that demand emanates from man, and that man is a bundle of habits, whims, fancies, prejudices, likes, tastes, wilfulness, and vagaries. Upon such an unstable foundation every market rests. Amid all fluctuations, however, there is some constancy; some rules, some principles are there. There are elemental needs which must be met. There are staples to be marketed.

A final point should be kept in mind. Demand is a demand for something of a particular kind, at a particular time, and in a certain quantity. Any shift in this demand will be reflected in the commodity to satisfy it. It is, therefore, impossible to study the characteristics of a commodity wholly apart from the demand. There is a continued interaction between commodity and market. One cannot logically be analyzed independently of the other. The "uses" of a commodity means only the demand for it. With this false step in logic clearly in mind we turn to a detailed study of the market centers.

**44. Geographical Location of Market Centers.**—There are in general three kinds of market centers, namely, the local market, the primary market, and the terminal market. The local market is the one with which the producer is in immediate touch; it surrounds the productive area; it requires only the haulage which the producer himself can furnish. The type is not wholly distinct but is characterized by direct contact between producer and retail dealer or consumer. The trade organization of this market is of the simplest type.

The primary market is a concentration point, where commodities are assembled in small lots, for carload or boatload shipment. Here are the elevators, the cold storages, the warehouses. These are the centers of reserve stock, where the commodities are gathered at harvest time and from which the supply is distributed through the year.

The terminal market is still more dimly defined, but may be called the market center at seaboard or at the national border. From it the commodities pass out of the country. At that point domestic trade ceases and foreign trade begins.

It is important to locate geographically each type of market center for a given commodity. It is a part of the analysis of demand to define and to account for market centers. The local demand has its peculiar phases; so have the concentration points and the terminal markets. Demand makes itself felt through the trade organization of each type of market center. Some centers, either because of an early start, because of superior advantages, or because of fortuitous circumstances, have specialized in certain commodities. This holds true even though ultimate consumption takes place elsewhere.

Wool, although grown over a wide area, and therefore having a great many local markets, illustrates a concentration of primary markets. In the East these are Boston, New York, and Philadelphia. In the West are Portland and San Francisco. It is to these centers that the manufacturers' buyers naturally go. Here are the great wool warehouses wherein a supply is stored to satisfy the needs of the trade all the year round. In the Middle West are the "transfer points," Chicago, Omaha, and Saint Louis. A warehouseman in Chicago, some years ago, undertook to develop that city into a wool market. He sent buyers out West and established contact with the growers. Within two or three years he had lost some $50,000 and then gave up. It was not possible for him to divert the trade: he had nothing to offer.

> The general stream of commerce seeks the outlet of least resistance. Historical forces have much to do, however, in changing the course of the commercial movement. After much effort the political obstacles which stood in the way of the free navigation of the Mississippi River were removed and that highway became the natural outlet for the surplus farm products of the vast interior plains. But the war between the States closed that outlet and the main movement thenceforth sought egress by way of the lakes and the Eastern trunk lines to the sea. . . . The diversion of grain traffic from Buffalo to Montreal is an illustration of this same principle that economic foresight rather than the advantages of nature determines the course of traffic.[1]

Cotton illustrates the concentrated productive area, with a strong tendency toward a one-crop system. As ultimate consumers there are the Southern mills, the Northern mills, and the foreign mills. Where are the trade centers? Most small villages afford a local market. From these about half the cotton goes to compress points and the rest to interior concentration points. There are thirty-five or more of these interior market centers, the largest of which are Houston, Memphis, Saint Louis, Augusta, Atlanta, Cincinnati, Little Rock, Montgomery, Columbia, Shreveport, and Dallas. In the season of 1911-1912, 47 per cent of the entire cotton crop went through twenty-eight of these market centers.

The functions of such market centers are as follows:

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[1] Report of the Industrial Commission, 1900, vol. vi, p. 126.

(1) they are the collection points, where the large exporters of cotton can hold their purchases; (2) they furnish the mechanism for central cotton markets; (3) they provide the necessary facilities for storing, weighing, compressing, sampling, grading, inspecting; (4) they have established a news bureau for prices.[2]

But there are two other kinds of cotton markets. More than half the cotton grown in the United States and consumed within the country, goes to mills located in the productive area. The rest goes to Northern mills. Sixty per cent of the total crop is exported. To reach the Northern mills and the foreign markets, cotton passes through certain inland centers called "northern gateways," or through cotton-receiving ports. The chief Northern gateways are Saint Louis, Memphis, and Cincinnati. The principal cotton ports are Galveston, New Orleans, Mobile, Savannah, Norfolk and Newport News, and San Francisco.[3]

The functions of cotton ports are: (1) they serve as shipping centers, with docks, wharves, transshipment facilities; (2) they afford points of concentration; (3) they offer open markets. These are the true types of terminal markets.

The market for milk is the city or town; the larger the city, the more important the market and the more complex the problem. In the United States, the most difficult problems are connected with New York, Boston, Philadelphia, and Chicago. For eggs there are local markets everywhere. Chicago is the largest primary market, or concentration point. Eggs that are shipped into that city are reshipped both east and west, and are also held in storage. New York is the real terminal market. For such a commodity as crushed stone, there is, practically speaking, only a local market. It is very definitely limited by transportation cost. It rarely pays to carry crushed stone more than 200 or 300 miles. Pig iron has almost altogether a local market. This type of market may be illustrated by the situation in Colorado and in Pittsburgh. Birmingham, Alabama, may be called a primary market. Chicago is the chief market center for anthracite coal west of Buffalo. The sole market for sugar beets is the sugar-beet factory; and it is necessary for this factory to be located near the beet fields, because raw beets are perishable, and heavy and bulky in comparison with their value.

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[2] See Huebner, *Agricultural Commerce,* p. 117.

[3] These centers should be carefully located on a map and their locations explained.

The market for leather is determined by the shoe and glove industries. For these industries there are two regions of concentration, one in the far East, the other in the Middle West. New England produces a large percentage of shoes, and gloves are made at Johnstown and Gloversville. In the Middle West the demand for leather is largely concentrated in Chicago, Milwaukee, and Saint Louis. The shoe industry absorbs 86.3 per cent of all the leather; the glove industry consumes 10 per cent. The chief market centers for cane sugar are New York, Boston, Baltimore, New Orleans, and San Francisco. The primary markets for peanuts are Suffolk, Norfolk, Petersburg, Franklin, Wilmington, Fort Worth, and Houston. The largest receiving port for tea is Tacoma, then in order New York, Chicago, and San Francisco. The chief market centers for lead are St. Louis, New York, and London. St. Louis is the trade center for aluminum. The meat-packing centers are well known.

When raw materials and foodstuffs move to market they reach first a local market, then the primary markets, or concentration points. Some part may be finally consumed in each of these. The rest will pass on to the terminal markets. The ultimate consumer of these things may be either a factory or an individual, but generally from the producer's standpoint, interest in the product flags when it passes beyond his control into the hands of a dealer. There is here a pretty clearly marked distinction between raw materials and finished products. The manufacturer is becoming more and more interested in the consumer demand.

**45. Boundaries and Overlapping of Market Areas.**—Each market center has its logical boundary determined by its marketing advantages. It may also dominate a wider area through tradition or reputation. The two chief influences to set the boundary stakes to a market are transportation and marketing facilities. Cotton may flow to Galveston or to New Orleans, wherever the best marketing facilities are. A great municipal warehouse, with ample docks and a belt-railway system, has been recently constructed at the latter place. A very slight change may send wheat from Kansas to New Orleans, rather than to Chicago, on its way to seaboard.

An industry tends rapidly to stabilize itself in relation to markets. Channels of trade are quickly worn. The marvelously sensitive system known as *arbitrage* is a powerful stabilizing factor, speedily restoring the equilibrium. Taking the country as a whole for a commercial unit, there will be found a great number of price centers for each commodity. The Department of Agriculture has estimated these price areas for wheat. Controlling each price area is a market center. But the boundaries are not clearly defined; a relatively broad twilight zone exists. It happens, too, that these boundaries tend to overlap. This is characteristic of the cotton-market centers. Boston, New York, Philadelphia, and Baltimore are overlapping market centers for many commodities. Chicago and St. Louis, and Chicago and Minneapolis overlap for many commodities.

Commodities may slip past their "natural" markets to more distant ones. Cattle from the far West may be shipped to Chicago; they are sometimes shipped 1,000 miles. Some livestock still drifts eastward to packing centers in New Jersey, even though it is more economical to ship dressed meat. Refrigerator cars filled with fruit may be diverted *en route* to points quite different from the original. This splendid flexibility makes for a more efficient market. There are no political barriers to stop trade within the United States; it is a single free-trade area. Physiographical barriers have been largely broken down by an effective transportation system. Supply and demand work more freely over broad stretches of the country; market areas are thus extended; there is further overlapping and need for readjustment.

**46. Market Competition.**—There are two kinds of market competition, real and potential. A market center is held in line by the fact that its neighbor stands ready to invade its "natural" territory. Also, through the overlapping referred to above there is real competition. This kind of competition may run on the basis of price, quality, or service. As one approaches the margin of a "natural" tributary territory to a market center, the competition in price becomes keener between the centers.

Within the market center there is usually intensive competition. Take the livestock markets, for instance. Within them may be found the large packers of the Middle West, the smaller packers, the wholesale slaughterers, the Eastern packers and slaughterers, the exporters, the stockers, and the feeders. Within a given market area there is competition for the supply of milk, as "raw" milk, for condensed milk, evaporated milk, and milk powder. Makers of cheese and ice cream also contend with milk dealers. Within the market, as well as between markets, there is competition.

Among local merchants the competition for eggs, which are usually bought by count, is wholly on the basis of price.

All eggs are assumed to be equally desirable, regardless of quality or size. In crushed stone, the competition is wholly on the basis of price. Salt is usually competed for on a price basis, although it has been possible to give distinction to it by boxing it and making it pourable. Staples generally are bought and sold on a price basis.

**47. Consumer Demand in Relation to Market Centers.**—Emphasis has here been placed upon the market center as the market for raw materials and foodstuffs. When these commodities have reached the market center they have traveled only part of their way to the consumer. The demand of the market center is always guided and controlled by the consumer demand. It is the shifting in the demand that causes readjustments among market centers. Cincinnati was once the great central livestock market. The market was later transferred to Chicago, and now bids fair to pass on westward. Chicago was formerly the greatest wheat market. Now Minneapolis has forged ahead. South Bend was once a much greater lumber market than it is to-day. As the peoples shift, the markets shift.

This consumer demand affects not only the quantity but also the quality of the product. Milk is coming more and more to be sold on the basis of quality. As purchasing power increases, consumers demand a higher quality of product. Through the mechanism of market centers the change in consumer demand is carried to producers.

**48. Character of Market Demand.**—The demand for raw materials and foodstuffs has many important characteristics. Once more each commodity will develop its own peculiar problems to be solved. These will require special study.

One of the first inquiries to make is, what is the size of the market area? It may be merely local as is true of cement, crushed stone, sugar beets, sand, and gravel. This does not mean that there is no demand elsewhere. It indicates that some factor definitely and finally limits the area. In the instances cited, it is the cost of transportation. There used to be only a local market for perishable products. Transportation facilities have made possible a much wider market for them. Or, take the case of milk. Its perishability, in general, limits each market area, but special circumstances have arisen, such as a boycott by producers, under which milk has been carried from the vicinity of St. Louis, and some has been brought a 1,000 miles from the New York territory to Chicago.

There are other markets too broad to be called local, but yet which do not pass beyond the limits of the state. Some businesses are incorporated to operate within the state. The artificial—from the point of view of economic forces—boundaries of a political state, however, do not furnish any logical delimitations for a market.

The market area may broaden out to cover the entire country. Again, there are political barriers only to be overcome. Tariffs, agreements, duties may affect the area. But the saying, in general, is true, that trade knows no national limitations. Treaties and tariffs may hamper competition and for a time set narrow bounds to the market, but all such obstacles have been overcome in the past. There are, of course, certain national tastes, habits, traditions, which affect the frontiers of a market, just as within a country there are religious beliefs that affect demand.

Many commodities, and the number increases, enjoy an international market. Among these are gold, silver, copper, wheat, cotton. While the demand for these as raw materials is concentrated in the manufacturing establishments, these in turn are affected by the universality of demand for the products. There will tend to develop a world-market center.

On the whole, political boundaries do not coincide with market areas. Economically speaking, political boundaries are accidental and artificial. Nevertheless, they may have important influences and should be studied in connection with each commodity.

Politically, and in the administration of matters of purely local concern, the forty-eight States may retain their entity. But economically the country will consist of six great regions, each an empire in wealth and territory, each homogeneous in point of business and industry and all bound together by a network of a quarter million miles of shining steel. The scalpel of community interests would divide our national body into the Eastern Region, the Southern Region, the Lake Region, the Central Region, the Southwestern Region, and the Western Region.

For all practical purposes each region embraces a territory in which the industrial character of traffic, places of outlet, and general conditions are homogeneous. The Eastern Region comprises the great industrial section of the country—the textile mills, the shoe and leather manufactories, the iron and steel business, and the coal and oil fields. The boundaries of the Southern Region encompass the cotton-growing, spinning and weaving industries, the iron and steel works of the South, general farming, fruit and tobacco belts. Within the Lake Region lie the vehicle and agricultural-implement industries and the mining and smelting districts of the Great Lakes. The vast empires of wheat, corn, and other grain and dairy farms are included in the Central. Our great sugar, rice, and cotton plantations and the stock-raising industry center in the Southwestern Region, while the grain and fruit belts of the Northwest, the cattle ranges west of the Rockies, and the fruits of the Pacific Coast are within the boundaries of the Western Region.[4]

**49. Character of Market.**—There is also what may be called the character of the market, from the point of view of ultimate demand. On this basis, there will be the city market, the town, or village market, and the country districts. Fertilizers are destined for the farm. Road materials are for the country roads. Food demand concentrates in the city. Each demand has its peculiar characteristics. As will be shown later, there is group individuality in demand that reaches in influence back to producer. It affects in the process the entire market structure.

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[4] See Chiquoine, *Public Ledger*, Philadelphia, Dec. 24, 1916.

**50. Historical Considerations.**—Just as production should be studied historically, in order to discover tendencies and thus afford material for discounting future changes, so the historical aspects of demand must be considered. Changes will develop, due either to (*a*) population movements, (*b*) a rise or fall in the standard of living, or (*c*) a shift in tastes, habits, or relative desires.

In the development of a new country immigration flows in and spreads out to all parts. By fortuitous circumstance the early ingress into the United States was on a "stern and rockbound coast." Later the fertile interior drained off the Eastern population, and then the West and Northwest attracted the people from the Middle West. Always market conditions have changed to adapt themselves to these population movements. Transportation, communication, and finance developed at the same time. Currents of trade in the past have been east and west; in the future they may be north and south. If so, market facilities will adjust themselves to the change. There may come a back flow, too, with its effects. These large movements within the country and even in the international market should be followed, and their effect upon the markets noted.

A standard of living is an indefinite thing, almost wholly relative in character. There may be at some point an irreducible minimum, but this is always and everywhere to be avoided. Standards of living rise with increased purchasing power. With such changes, luxuries become necessities, and new desires are awakened. These are reflected through market centers upon production. In a new country there are as broad movements in the standards of living as in population. Swift changes occur, also, in districts where oil is struck or where a new industry is developed; the running of a railroad through a new country has a similar effect.

Waves of prosperity follow population movements. As the "Star of Empire" takes its westward way, there may be left behind a deflated business. With the old prosperity has departed the requisite purchasing power.

The standard of living in such districts will sink to a lower level. The market is changed; demand is altered. Effects of this sort must be watched and provided for.

While a great volume of consumer demand flows steadily on from year to year, there are many shifts in tastes, habits, and wants. Unless a manufacturing plant can readjust itself to such shifts, it will no longer be a market. One plant had expanded tremendously during the war to meet the demand for war materials and turned to the making of hardware implements afterward. There was no lessening of this market for materials. A planing mill shifted to the making of fruit crates that were especially needed at the time. By this shift the mill became an even greater consumer of lumber than before. The substitution of soft drinks, cider, candy, and tobacco for "strong drink" has affected the marketing of materials. The development of a demand for corn products has become great enough to have an appreciable effect on the immense yield of that grain. The widespread use of aluminum utensils has greatly affected the marketing of the raw materials. Asbestos is entering into an increasing number of articles and the marketing of the raw material is affected. The unusual demand for silver in the arts and for coins has revived old sources of production. The unprecedented demand for nitrates caused the development of a new source from the air. A great number of modern inventions call for petroleum products. It is a part of the problem of marketing raw materials to keep in touch with these changes.

In this connection it is proper to consider the subject of substitutes. Substitution may take the form of a new source or of a new substance. That is, a substitute may be developed as a result of a more complete utilization of by-products, as illustrated in the meat industry, and in the petroleum industry, or an entirely new material may be found adapted to an established demand. The latter condition is frequent. Platinum may supplant gold in certain ornaments; wood fiber and nettles may take the place of cotton and wool in textile manufacturing, as in Germany; a synthetic rubber may be made. The instances might be greatly multiplied. Every such change will obviously reach back in influence through the market. Thousands of active minds are seeking persistently, tirelessly, to develop new substitutes of both kinds. Scientific knowledge is becoming a more and more fruitful source of substitutes. It is not a process to be condemned, but to be watched; it is an active element in the market.

The purpose in following the historical development of an industry is to be in a position to anticipate changes. Business is too prone to succumb to easily-established tradition. A broad view of market development is the best possible corrective for hidebound tradition. It gives background, perspective, confidence, and a superior basis for judgment. The historical sense of the American business man needs nurturing. Commercial and industrial history contains many an important lesson; from the accumulation of experience will emerge at last sound and dependable principles of business. It has a strong practical bearing, too, in that such a survey will reveal the broad changes discussed above. As early as possible, it is necessary to mark the trend toward a general increase or a general decrease in market demand, or whether, indeed, the demand is a fairly stabilized one and why.

**51. Climatic Considerations.**—The climate is a most important commercial consideration. This is true not only for the great farm products which the uncertain and uncontrollable weather changes make so speculative, but also in only a less degree for all commodities. It is said that in Boston, if in a series of hot days the wind veers to the east, the demand for milk falls sometimes by 20,000 quarts in a single day. The effect upon the demand for ice of a cool or hot summer is obvious. Many other climatic considerations are almost equally as influential, if not so obvious. Coal, gas, wood for heat; building material for shelter; clothing material to wear—all of these depend directly upon climatic considerations. In other cases demand fluctuates directly with climatic changes. This factor may be of no particular or of vital importance. It is the burden of each special investigation to determine this fact.

**52. Seasonal Considerations.**—There are seasonal factors in demand as well as in supply. These, too, must come under the survey. Coal for winter, ice for summer, are obvious illustrations. Material for woolen clothing when the weather grows cold; cotton material for hot weather; the whole series of seasonal trades—all are in the same category. It is well known that this element in demand complicates the problem of industrial management, of unemployment.

This fluctuation in demand may be due either to changing needs or to other, external factors. Farmers may concentrate their buying after harvesting and selling the crops. The payday is a widespread and potent factor in demand variations. The manufacturer may wait until he gets an order before buying materials. This element in demand is well known and readily observed, although its importance is not often enough appreciated.

The burden of leveling out this concentrated or seasonal demand rests upon the market. It often happens that a seasonal supply of material is separated by six months from the peak of demand. This is true of cotton in the Northern climate. But this period allows the manufacture and distribution of cotton garments in time for the warm season. Wool shearing may come in the spring while the demand for wool clothing begins in the autumn. Ice is formed in winter while the peak of demand comes in the mid-summer. This lack of synchronizing is taken care of in the market organization.

Where the supply is readily controlled and regulated this is not so difficult. It is, nevertheless, practically impossible to get householders to buy their supply of coal for the winter until the "frost is on the punkin, and the fodder in the shock." Demand persists in being seasonal even though the recurrence of the demand is beyond question. The shock absorber over these bumps of demand and supply is the "trade."

**53. Financial and Market Relationship.**—As has been noted before, the two pervasive elements in the economic process are transportation and finance. The former will be especially considered in a later chapter, but something should be said here of the latter. Nothing can cut off demand more peremptorily than a financial panic. Finance is a most sensitive barometer of trade.

The financial situation may be affected by many different things. Among the most important is a crop failure. This disaster spreads quickly through the entire market fabric, just as when a stone is thrown into a mill pond. A new crop means renewed purchasing power among a very large group of consumers. The demand thus created acts through the market upon many kinds of materials. It is like a transfusion of new life-blood into the system. The reverse is true if there is a crop failure. A deadening influence spreads through the economic system.

Some trades, that is, some kinds of demand, are far more sensitive than others. The building trades are among the first to suffer, and the demand for building materials slumps quickly. The pig-iron trade is looked upon as a barometer because of its immediate and sensitive response to financial changes. This is because of its fundamental character; it underlies so many other industries. In general, luxuries naturally react more quickly and more violently than necessities; novelties more quickly and violently than staples.

Each commodity will show its own peculiar traits. Demands are pyramided upon demands. Business is an intricate, correlated and interrelated system. A famine in India may affect the silver market in the United States. A stoppage of the importation of human hair from China may have an unexpected influence upon the cotton-seed industry in this country, because this material is essential to the making of press cloth for straining cotton-seed oil. It is into this complex but fascinating maze that the student of marketing problems must plunge.

How does the demand for a given commodity act in a crisis or a panic? Those last days of July, 1914, at first stunned the Chicago Board of Trade. Demand withered away like a tender plant before a wintry blast. Then suddenly it sprang to life again. A frenzy of buying succeeded stagnation. These wild periods in a market are largely due to ignorance. He who has made himself familiar with the conditions of supply, who has carefully analyzed demand, can weather such a period calmly from the simple fact that he has already discounted the changes.

**54. Conclusion.**—The complement of an analysis of the commodity is an analysis of the market. As applied to raw materials and foodstuffs, the study of demand may be concentrated in market centers through which the ultimate, consumer demand makes itself felt. This means a study of the size, location and character of trade centers. Raw materials flow from their source to the mill; for them the mill is the market. Foodstuffs are drawn from regions of surplus to regions of deficiency. The regions of deficiency vary in intensity directly with the density of population. The larger the cities, the larger the market. With this survey completed, one is ready to proceed to an analysis of the problems that arise in bringing the supply into contact with the demand.

### SUGGESTIONS FOR STUDY

The discussion in this chapter should be applied to the commodity selected by each student for research work. For class-room discussion the following assignments will serve:

1. Locate on the base map already used for the productive regions, the chief primary and terminal markets for (*a*) cotton, (*b*) wheat, (*c*) livestock, (*d*) petroleum, or other commodity.

   *References:*

   *United States Atlas.*
   Thirteenth Census, vol. v, x, p. 39-, 337-, 657-.
   Reports of U. S. Geographical Survey.
   Huebner, *Agricultural Commerce,* pp. 94-100, 116-26, 50-61, 164-170, 181-187.

2. Study these market centers in reference to productive area, to centers of population.
3. List in order of importance the commercial reasons for the location of the markets. Do you find evidence of "artificial" markets?
4. Try to determine the "natural" boundaries for these market areas.
5. Is there an overlapping of market areas?
6. What are the most important climatic and seasonal considerations affecting each commodity studied?

7. What are the effects of population movements upon the demand for each commodity?
8. What elasticity is there in the demand for each commodity? How evidenced?
9. Is there evidence that production and market demand are approaching an equilibrium?
10. In consideration of the facts secured, what is your judgment as to the future of the market centers?

# CHAPTER IV

## TRADE ORGANIZATION

Given a commodity and a market, what is the mechanism that has developed for bringing the two together? In any complex society this bringing of supply into contact with demand requires specialized service. This specialized service will develop its own peculiar type of machinery for performing the necessary tasks. This machinery is the trade organization.

At the outset, it must be kept clearly in mind that a trade organization is not a fixed or permanent thing; the existing organization is not the best or the worst possible, but is an attempt to do a required service effectively. Business is in its very essence selfish, in that it runs upon a basis of profits. The men behind the trade organization are not philanthropists; they are in business for pecuniary gains; they will demand a reward for their services. The task of a business investigator is to inquire whether or not their services are real, what the nature of these services is, what the reward paid for them, and what defects are apparent in the mechanism that has developed to facilitate distribution.

**55. Functions and Institutions.**—A distinction has already been drawn between functions, the services necessary for distribution, and the institutions with which these functions are associated. The terminology in this connection is unfortunate, because the language may carry a variety of meanings. But it should be understood at this point that the following discussion of the trade organization for marketing raw materials and foodstuffs will be based chiefly upon a functional analysis.

**56. Market Functions.**—What are the services to be performed in carrying commodities to market? They have varied at different times in character and in importance. New ones have emerged as industrial society has grown more complex. Now and again a phase of the distributive function has been isolated and specialized. The rudiments of practically all services were present in the simplest and most primitive kind of trade organization. The identification and specialization have taken place more or less slowly and the whole process has been so matter-of-fact, so natural and commonplace as not to have drawn any special attention to itself.

The present distributive system, then, is the result of growth and of gradual modifications. It is not now and never has been fixed or stable. Through the years of competition, there has been a slow, relentless tendency to eliminate uneconomical methods. To-day there is visible everywhere evidence of change. This is a sign of progress, for without change business stagnates. Two contending forces are at work, one toward greater specialization, another toward a concentration of functions. The banker, the transporter, the wholesaler, the retailer, the insurer, all have taken unto themselves specialized functions. At the same time, as the distributive system grows more complex, "the middleman tends, by the development of his own efficiency, to eliminate himself from trade."[1]

It will be worth while to note the effects of this double tendency in business.

A careful study has been made of the rise of the middleman in English trade. From this historical point of view the following general comments on market functions have been made:

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[1] Westerfield, *Middlemen in English Business,* p. 127.

> Commerce consists in the equalization and distribution of surplus goods as between persons in different places and different times. These ends are accomplished by carriage, storage, foresight, communication, and exchange. The agents of these acts are the merchants, tradesmen, and brokers. Of two persons or two places, the one receives a succor which is relatively necessary to it, by exchanging a surplus which is relatively useless to it against the goods of which it is needy.
>
> These functions may be grouped in two classes. The middleman buys with some distant or future market in view. As far as the future market is the objective one, the business is purely speculative and rests on the control of capital. This dealing in time-markets may be regarded as the "capitalistic" function. But when this future market is also a geographically distant one, a second function is called into play, namely, the discovery, study, and fostering of that market and the connecting of the local and distant markets. This dealing in place-markets may be called the "connective" function. It is concerned with the methods of business connection and the means and use of communication.[2]

The functions isolated by this analysis are: "carriage," that is transportation; "storage" or warehousing; "foresight," by which is meant presumably speculation; "communication," whether secured by letter, wire, or travel; and "exchange," or the actual buying and selling. While these terms are not mutually exclusive, they mark a beginning of the separation of functions. The distinction made between time-markets and place-markets, between the "capitalistic" function and the "connective" function is well worth remembering.

The results of another attempt to enumerate the functions involved in marketing are given below:

> The services performed in the marketing process, including practically every item in the detailed expense account of a merchant or of the selling organization of a manufacturer, can be

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[2] *Ibid.*, p. 349.

classified under one of the following heads: (1) assembling; (2) storing; (3) assumption of risks; (4) financing; (5) rearrangement; (6) selling; and (7) transportation. The only important exception to this classification is the expense connected with accounting and office management, or what Shaw calls "the facilitating activities" of a business. But these are purely incidental to the primary functions enumerated above, and may properly be considered as assignable to, or incurred in connection with, their performance.[3]

The analysis is here carried several steps further. It is found necessary also to define very generously some of the terms used. "Assembling," for instance, does not at once convey to the mind the fact that it "involves all the services connected with buying." It would never occur to the casual reader to make it the complement of selling. Nor does the significance of "rearrangement" make itself immediately intelligible. As a matter of fact it "involves sorting, grading, breaking up large quantities into small units, packing, etc."

These are noteworthy attempts to isolate the functions that must be performed in getting goods to market. It is not with the thought of analyzing more keenly or deeply, but with a desire to present the exposition more clearly, that an independent list of functions is made here. This discussion of the marketing of raw materials and foodstuffs aims at emphasizing the control of and the assumption of risks for these commodities in the process. It will follow the topics as given below.

**57.** *The Middleman.*—This discussion will define the most important types of middlemen and will describe their functions. Among middlemen there are the buyers and sellers in the local market and the buyers and sellers in the wholesale market. The local buyers, the commission merchant, the broker, the forwarder, the general consignee, and the "dealer," or retailer are all middlemen. Attention will be centered upon the wholesale market and its middlemen.

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[3] Weld, *American Economic Review,* June, 1917, p. 306.

58. *The Transportation Function.*—The point of view here is a consideration of transportation as a commercial problem. What the general business man needs to know of rate regions and rate structures, of rate schedules, of special cars, of routing and demurrage, of trolley lines and the truck service, will be touched upon. Something will be indicated, too, of the importance of the transportation factor in the marketing of raw materials and foodstuffs.

59. *Organized Exchanges.*—There will be a discussion of the function of exchanges, as well as of their development and organization. The different kinds of exchanges, so broadly treated as to include the organized produce market, the stockyards, the butter and egg board, the auction, and the iron and steel institute, will be briefly described. It will be necessary, also, to indicate the influence of speculation through exchanges upon the marketing problem. Here, too, belongs a discussion of the coöperative marketing movement.

60. *The Warehousing Industry.*—The remarkable development of the warehousing industry will be described. An analysis will be made of the storage function in modern business. The types of warehouses, such as the general mercantile warehouses, the bonded warehouses, the grain elevators, cold storages, stockrooms, will be indicated. There are definite problems, mechanical, commercial, and legal, connected with the warehouse. These will be touched upon. The place of the warehouse in commercial organization will be discussed.

61. *Commercial Grading and Inspection of Commodities.*—The whole realm of establishing grades, of inspecting and weighing commodities needs thorough investigation. Something has been done already in determining the stand-

ard grades of two or three great staple products; industrial chemists are making progress with certain minerals and metals. Scientific commercial standards are yet to be set. In this discussion the problem will be outlined, and the method of approach will be suggested. There will be description of the machinery for grading, weighing, inspecting; of the scientific tests for setting standards; of the relation of the government to commercial grading; of the effects upon the commodity and upon the commercial organization. The relation of the consumer to standard grades will be discussed.

62. *Market News.*—The function of market news in the modern system will be taken up, and its fundamental character will be demonstrated. The thesis to be developed is that business is a going concern, that prices are not made from the ground up day by day, that to-day's price is yesterday's price modified only as a result of some information from the field of production or consumption, *i.e.*, market news. Something will be said of the machinery for collecting and disseminating market news, by the government and by private agencies, something of the control of trade information, the discounting of the future on the basis of market news, the transformation of business facts into market news, and the relation of market news to competition. The possibilities to use and to abuse trade information will be dealt with.

63. *Market Price.*—The analysis of market price will be taken up. The function of market price will be shown, and the price factors and influences. There are prices at the local markets, the primary markets, and the terminal markets. There are wholesale prices, retail prices, and consumers' prices; there are methods of determining and of quoting prices; there are price "steps" or intervals, and there is the "spread" between the price to the producer and the price to the consumer. All of these things will

come under survey. It will be shown how price is the axis of commercial organization. The movement toward a standard price through trade organizations will be traced. Our experience with price fixing and our conception of a "fair" price will be discussed.

64. *Financing Distribution.*—A brief discussion will be given of the financial instruments used in marketing, such as the bill of exchange, the bill of lading, the warehouse receipt, and the trade acceptance. There will be a summary of the function of credit instruments. The method of shipping on consignment will be analyzed, and the costs of marketing will be discussed.

It is on the basis of these functions that the discussion in the succeeding chapters will run. One and all, these are fundamental marketing functions; they apply to the marketing of finished products as well as to the marketing of raw materials and foodstuffs. This functional analysis, however, is made in the section dealing with raw materials and foodstuffs because of expediency.

There is greater functional specialization in marketing farm products than in marketing manufactured products; in other words, farm products pass through the hands of a greater number of successive middlemen. Furthermore, there is a distinct tendency in the selling of manufactured products toward the "elimination of the middlemen," or rather toward the taking over of the marketing functions by producers—a tendency that is not apparent in the handling of farm products. In the farm-products trade, for example, there is usually a country shipper—a middleman who has no counterpart in the manufactured-goods trade. Also the wholesale distribution of farm products is commonly divided between two agents—the wholesale receiver, or commission merchant, who assembles large quantities from various and far-away localities; and the jobber, who sells in small quantities to hundreds of retailers. In the wholesale trade in manufactured products there is no such important division between two functional specialists, although the commission house, manufacturer's agent, and broker, described above, sometimes appear between manufacturer and wholesaler.[4]

**65. Trade Organization Modified by Commodity.**—Every trade organization has its peculiar devices to care for the peculiar needs of marketing the commodity or commodities handled. Cotton, which is grown by about 1,700,000 growers, ginned by 25,000 ginneries, stored at 2,600 public storage places, and consumed by 2,100 establishments, has one of the most complicated of the American farm-crop producing systems. Coal, iron ore, petroleum, salt, aluminum, copper, lead have relatively simple marketing systems. One is simple and the other complex for an economic reason. It obviously is easier to control output, to adjust production to market demand under centralized direction in the mining of ores and minerals than it is in the raising of farm crops. There is no more uncertain, speculative business in the world than handling farm products. The marketing process, therefore, is divided and subdivided until a great cumbersome organization is the result.

As market conditions become stabilized the trade organization tends to become simplified. When risks are great and marketing problems are difficult and complex, the trade organization tends to develop in complexity. The marketing of milk is simple; the marketing of wheat is complex. The former has for each market, itself of limited area, a narrowly limited area of production; the latter a far-flung productive area and an international market. Wheat is affected in production and in its markets by world forces. Milk is affected predominantly by local forces.

Because a trade organization has a definite series of problems to solve, such as problems arising from a certain commodity or a related line of commodities, it must adapt itself to meet them. Hay has a loose-jointed trade organization because of the character of the commodity and because there are certain widely divergent demands. Each demand has created its own type of marketing machinery. The marketing of eggs gives evidence of becoming a subsidiary activity of the meat packers. One reason is that there was already in existence a system of marketing machinery which could be readily and effectively adopted for handling them. In crushed stone there has lately been a great increase in direct selling, because dealings have been more commonly in carload lots.

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[4] Weld, *American Economic Review*, June, 1917, p. 316.

The trade organization for any given commodity will be affected by:

1. The size of the productive area.
2. The character of the commodity.
3. The location of markets relative to the productive area.
4. The character of the demand.

**66. Strategic Points in Marketing.**—A recent writer has said that in the Middle Ages there were Crag Barons, who built the fortified castles on crags overlooking the main highways to market. From these castles they sent down their armed retainers to stop every passer-by and demand a toll before granting permission to go ou. To-day, he added, there are no longer Crag Barons, but in their places are Bag Barons, who have thrown a fence about the markets and demand toll of every passer-by. Bags and Crags, he avers, have the same effect on Rags.

This analogy was used against the large corporations. Whatever truth there may be in it, the figure does call attention to an important fact. Every commodity on its way from producer to consumer passes certain points where it is most vulnerable to attack. These are strategic points; that is, places at which control of the volume of production or of the market is possible. This means that certain functions are essential and can be performed only by a certain means or at a certain place. Transportation and finance have most often probably been the strategic functions. The producers of wheat still retain their animosity toward the railroads from the period of the Granger movement. When the railroads were declared public utilities, the elevators became strategic. To defend the producers against these, there was passed in Illinois the Warehouse Law declaring all warehouses to be public utilities, and the farmer's elevators were built. The oil pipe-lines gave the Standard Oil Company such a marketing advantage that they too were declared public utilities.

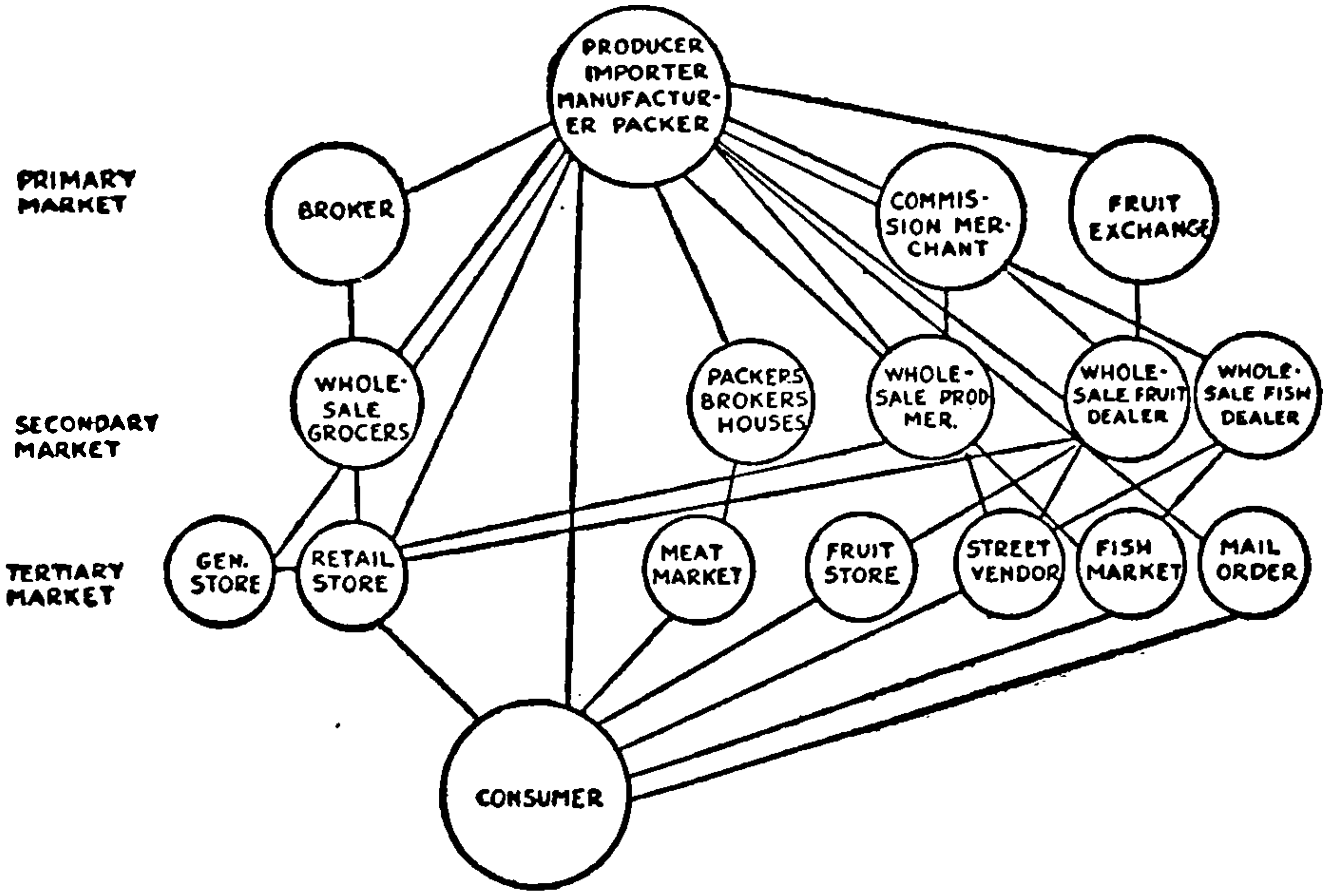
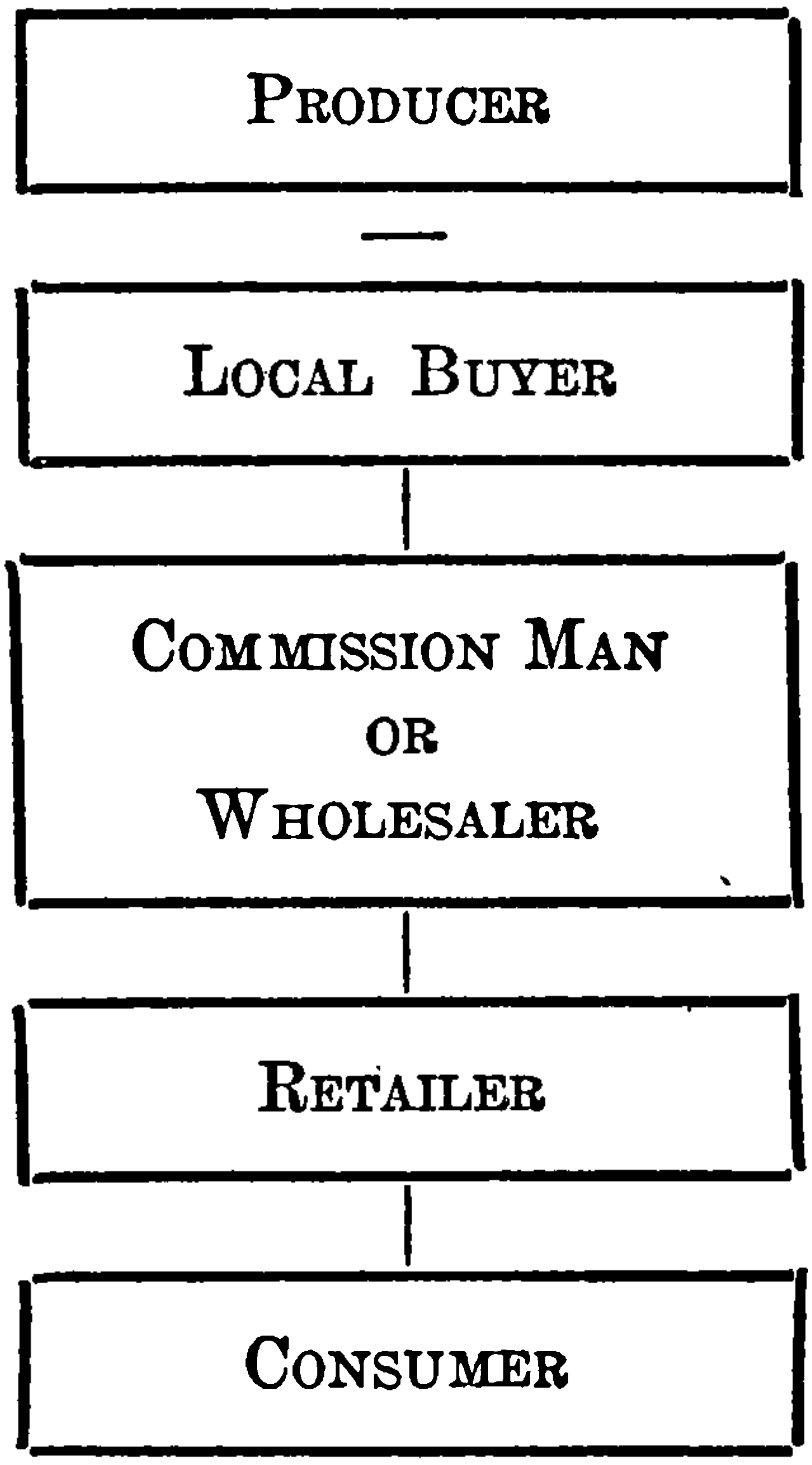

PRODUCER IMPORTER MANUFACTURER PACKER
PRIMARY MARKET
BROKER
COMMISSION MERCHANT
FRUIT EXCHANGE
SECONDARY MARKET
WHOLESALE GROCERS
PACKERS BROKERS HOUSES
WHOLESALE PROD MER.
WHOLESALE FRUIT DEALER
WHOLESALE FISH DEALER
TERTIARY MARKET
GEN. STORE
RETAIL STORE
MEAT MARKET
FRUIT STORE
STREET VENDOR
FISH MARKET
MAIL ORDER
CONSUMER

CHART OF CHANNELS OF FOOD DISTRIBUTION

In every marketing organization, there are these strategic points. It may be the refrigerator car, as in the case of meat and fruits; it may be the jobbers in the case of bituminous coal or the mine operators in that of anthracite; it may be the jobber and finder, as in leather; it may be the warehouse man, as in wool; it may be the exchange or the control of market news. Whatever and wherever these vulnerable points are, there will always occur a struggle for control and of defense.

**67. Trade Organization Chart.**—A sufficiently broad survey and detailed study will furnish data for constructing an organization chart for the marketing of each commodity. This chart, if carefully done, will reveal the points of advantage in the marketing process. The chart on page 70 is an attempt to show the main food sales channels from the source, the producer, through the importer, and the manufacturer, or the packer, to the consumer.

The typical organization for farm products has been outlined as follows:



MARKET ORGANIZATION CHART FOR FARM PRODUCTS

This organization chart shows only the chief functionalized middlemen and not the institutions which have grown up around them. A more nearly complete diagram would contain transportation, storage houses, exchanges, ginneries, refineries, blenders, graders, financiers, etc. The warning should possibly be sounded to the effect that the diagrams here given were constructed for particular emphasis.

68. **Types of Trade Organization.**—Some examples of trade organizations are cited here. The sketch in each case gives merely the outline, the critical problems not being even indicated.

### BEANS

Beans must be considered both as a truck crop and as a dried product. Beans for immediate consumption in a green state, as snap or string beans, are extensively produced throughout the entire trucking area. They are sometimes sold in a limited way to local buyers or shippers, sometimes handled in connection with other truck crops through coöperative organizations, but the great bulk of the crop is marketed through shipment on consignment, except in those regions where extensive canning operations are conducted. Beans for canning purposes are handled much the same as are tomatoes and peas. They are purchased by the canner at a stipulated price per unit of measure.

Dried beans are handled in much the same manner as other grain crops. Local dealers who are provided with suitable warehouse facilities and cleaners usually purchase the rough beans on a clean-bean basis from the growers, the cleaning, grading, and distribution being entirely out of the hands of the producer. The bean dealers are thoroughly organized and in close touch with the distributing markets. Growers, however, have up to the present time proceeded on the basis of independent action. There is no doubt that coöperation among growers would result in advantages, particularly in the sale and distribution of their crop.[5]

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[5] U. S. Department of Agriculture, Report No. 98, "Systems of Marketing Farm Products at Trade Centers," p. 33.

## BROOM CORN

*Methods of Marketing.*—In the small area in Illinois which produces the larger part of the standard brush, production has continued so many years that a very uniform product is derived from year to year and the method of marketing is a simple sale to buyers for the large factories or commission firms. In the Southwest buyers are stationed regularly in the larger centers and purchase the brush from the wagons as it is hauled into the towns.

It is the practice of some manufacturers and commission houses to contract for the growing of certain areas at a certain price per ton. This practice, however, has very frequently resulted in the breaking of a contract and even in litigation. It is charged by the contractors that the growers commonly break their contracts when the market advances above the contract price and adhere to them very tenaciously on a falling market. On the other hand, the growers claim that in the event of a crop of poor quality they are unable to obtain the contract price from the firms with whom the contracts are made. There are as yet few, if any, local organizations of broom corn growers in regions tributary to the larger producing centers. This doubtless will come when the newer producing areas have been longer settled and there is more community of feeling and interest among the growers. This will result in coöperative purchase of expensive harvesting and cleaning machinery and perhaps in coöperative drying sheds. It may result also in the employment of a specialist to superintend the curing, grading, and baling of the crop.

Wichita, Kansas, is probably the most important receiving and distributing point for broom corn in the whole country. Here are located enormous warehouses and many commission firms with buyers covering the entire territory of the Southwest, while Chicago, St. Louis, Kansas City, and, to a lesser extent, Oklahoma City, are also important centers for commission handling of the brush.[6]

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[6] *Ibid.*, p. 36.

## CHEESE, DOMESTIC SWISS

Most of the domestic Swiss cheese is made in southern Wisconsin. Factories are owned and controlled by companies of farmers, who empower the cheese maker to sell the cheese, or have a committee of their own membership to do the selling. The buyers of the domestic Swiss cheese are located in the small towns convenient to the producing territory. There were formerly a large number of independent buyers, but a number of these have recently combined to form one large company, the combination probably being made to eliminate competition. There are still a few independent dealers, one or two of which are doing a very large business covering the whole producing territory. Some of these dealers have close business connection with large New York and Chicago houses.

These buyers deal directly with the factory salesmen, usually buying what is called the "run of the shelf" at a fixed price. This means that all cheese of first, second and third quality is taken at the same or an average price. The buyer, of course, makes a close inspection of the cheese on the shelf before making his bid. This system of buying has the same evil tendency which creeps into all systems of handling dairy products in not paying a premium for a product of extra good quality.

Swiss cheese is held in the cellar or curing room of the factory for from six weeks to three months, where it goes through a ripening or curing process. Sales are at infrequent and irregular intervals. The committee of farmers will often hold the contents of their curing room for a number of months in the hope of better prices. There is no buying or selling on commission, the buyer always paying a flat price and buying on his own account. Cheese bought, as a rule, is delivered by the factory to the warehouse of the buyer, where it remains for irregular intervals. These warehouses are equipped with refrigerating facilities.[7]

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[7] *Ibid.*, p. 41.

## COTTON SEED

The peculiar commercial history of cotton seed has no doubt had a profound influence on the system of marketing it which has grown up in the United States. Thirty years ago some of the States of the cotton belt were still enacting penalty legislation to regulate the disposal farmers made of their seed, which, scattered on the public dumps and thrown into streams, constituted a serious menace to health. As late as 1880 less than 7,000,000 gallons of oil were produced in the United States. Twenty years later, in 1899, 93,000,000 gallons were made and in 1909 the production reached 157,000,000 gallons. In 1879 less than $4,000,000 were invested in the industry using this raw material, while by 1909 something like $91,000,000 capital unquestionably found profitable investment in the cotton-seed and cotton-oil industry. Let us first discuss the various methods by which the farmer disposes of his seed. It usually, perhaps in 80 per cent of cases, passes from his possession at the gin. Ginning in the United States is usually done at one of three places —(1) custom gins, (2) oil-mill gins, (3) privately-owned plantation gins.

The commercial ginner charges a flat rate per 100 pounds of lint for ginning, usually about 50 cents. The seed, of course, remains the property of the farmer, but generally custom ginners make a practice of buying and selling both cotton and cottonseed, hence in a very large percentage of cases the farmer parts with his seed to the ginner and for a flat price per ton—the price being determined chiefly by the selling arrangements the ginner has been able to make with the oil mill.

At the present moment farmers are selling seed in various parts of the cotton belt at prices ranging from $14 to $20 per ton. This diversity in price is not logically explainable in the great majority of cases on the basis of greater cost or difference in freight rate. In other words, two places equally distant from an oil mill with practically identical feight rates may be $2, $3, or even $4 apart in the price that is being paid the farmer for his seed. Indeed, the writer is familiar with primary markets where it is the regular practice to pay the large plantation owner $16 per ton for his seed, while the small grower and the tenant farmer receive only $14 for the same grade of seed from the same buyer. Likewise, in towns where both ginneries and oil mills are located very often the ginner pays $15 per ton for seed and at almost no added expense delivers it to the oil mill for $18 per ton. Nevertheless, if the individual farmer brings the seed to the mill himself he receives only the same price that he would have gotten at the gin. Local merchants to some extent also buy cotton seed and accept the same in payment of store bills, shipping to oil mills as soon as they have car lots.

The seed from plantation-owned gins is sometimes sold by the planter direct to the oil mills in car lots when a freight haul is concerned, but more frequently it is sold to local or traveling buyers.

There has been developed also to a small extent on large plantations, especially in the Mississippi Delta, the plantation oil mill. These are usually cold-process oil mills, and their crude product is sold direct to the refineries. In fact, it is believed to be impossible for the private individual owning a small oil mill to contract to have his own crude oil refined at any refinery in the United States. He is forced to sell. The profits in cottonseed-oil milling are undoubtedly quite ample, judging from the lump prices that are paid, the diversity in price between various primary markets, and the readiness of capital to engage in the business. There is real need for a disinterested investigation in the marketing of cotton seed from plantation to the finished oil product ready for consumption. The beginnings of such an investigation have already been made by the Office of Farmers' Coöperative Cotton Handling and Marketing, of the Bureau of Plant Industry. Considerable information has been gotten together and contracts have been established with several oil mills where coöperative work will be taken up as soon as additional funds are available.

The yield of oil per ton of seed may be roughly stated as between 35 and 45 gallons, though yields as low as 30 and as high as 50 are recorded each season. Variation in yield depends on seasonal differences and variety of cotton grown, character of weather, maturing time, etc.

A very little has also been done toward coöperative oil-mill building and operation, the members of the coöperative associations contracting to deliver all their seed to the coöperatively owned mill. These agreements are necessarily ironclad, as the competing oil-mill buyers would soon overbid the home concern and close it down by buying up its supply of raw material. The particular association best known to the writer paid its members $22.30 per ton for seed at the close of the season in a market that was only given $15. One frequently meets, in traveling about the Cotton Belt, buyers who go from gin to gin purchasing seed, both from farmers and ginners and others, and shipping the same to the oil mill they represent.

Primary markets have usually little competitive buying of cotton seed; the price is usually a flat price and all buyers pay pretty much the same. Farmers in certain seasons, especially this year, suffer because of inadequate supplies of freight cars for shipping seed. In several parts of Texas, during the present season, the writer found farmers compelled to haul their seed home, a number of miles, because buyers would not take it through lack of shipping facilities. Very few industries have fewer middlemen between the raw and finished product than does the cottonseed-oil business.[8]

## FLAXSEED

The production of flaxseed is confined almost entirely to the three States of Minnesota, North Dakota, and South Dakota. The demand for this grain is very largely from the linseed-oil mills, though small quantities are used for other purposes. Consignments on commission are made by growers of flaxseed in carload lots and shipped direct to the terminal markets. More frequently, however, grain is sold to local buyers for delivery to local shipping points. These buyers may be independent dealers, but more often they are representatives of milling companies with large interests at the terminal points. The principal terminal for flaxseed shipments is Minneapolis. Sales of flaxseed are seldom made at auction either in the region where it is produced or by agents or dealers in the large cities. This crop is not ordinarily sold prior to harvest. Sales are not usually made direct to the consumers, except where mills are located in the immediate vicinity where the crop is produced.

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[8] *Ibid.*, p. 47.

At a considerable number of towns in the three States where flaxseed is most largely grown, coöperative elevator associations have been organized. These associations buy the seed from members and, in some cases, from outsiders as well, and ship to terminal markets where the seed may be sold direct to the consumer, but is more often handled through a commission house. These coöperative elevators usually pay market price and return profits from their transactions to the members in the form of dividends. . . .

Flaxseed is seldom sold by the retailer in its original form, but, as already stated, is used almost entirely in linseed oil and its by-products. The linseed-oil mills purchase the seed either direct from the grower through local representatives in the region where the crop is grown, or from dealers at the terminal markets. The manner of handling this grain by commission houses is not different from the manner in which corn, wheat, and other cereals are handled. The principal purchases by mills and factories are made during the two or three months following harvest, after which time the seed is stored in local or terminal elevators until it is wanted for use. The items of expense in marketing include transportation from the farm to the shipping station, maintenance and running expenses of local elevators, transportation from shipping stations to terminal elevators or mills, maintenance of terminal elevators, and commissions.

Flaxseed is not ordinarily stored by the producer for any considerable length of time. It may be stored for a few days or weeks until it can be delivered to the local elevator, or in occasional cases it may be stored for a considerable period awaiting an advance in price. After it is purchased by local elevators it is quite often stored for a considerable period, this period varying from a few weeks to six or eight months.[9]

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[9] *Ibid.*, p. 49.

### FLOWERS AND ORNAMENTAL PLANTS

Cut flowers and plants are generally sold direct to the consumer or to the retail florist by the grower, and only surplus stock that cannot be disposed of otherwise is consigned to commission dealers. A grower, however, who is located some distance from a large city is compelled to dispose of his stock through a commission dealer. In such cases the stock is shipped to the dealer who disposes of the stock to the best advantage, charging a percentage for his services of from 15 to 20 per cent on gross receipts. Should the commission man be unable to dispose of the stock the grower loses the entire shipment, in addition to the express charges. Bills are settled monthly.

Frequently a retail florist will visit the growers' greenhouses, and if his plants give promise of yielding good flowers he will arrange to purchase the entire crop for the season, the length of season depending entirely upon the nature of the flowers; but it would generally mean the winter months, from October to April.

Nearly all flower growers dispose of most, if not all, of their stock by selling direct to the consumer, through the local markets or by having stores of their own.

Flowers and plants are either sold direct to the consumer, sent to commission dealers, or through local florists' exchanges. There are no coöperative selling associations. The stock handled by commission dealers is generally sold to retail florists only and not to the consumer.

Flowers are generally graded first, second, and third, depending on the length of stem, excellence of color, and size of flower. Grades are determined by mutual agreement among the florists and growers. No hard-and-fast rules have been adopted in regard to grading, therefore they vary materially in different cities.

Sales of flowers and flowering plants are heaviest through the winter months, from October to April, and are specially heavy at all holidays, such as Thanksgiving, Christmas, and Easter.

Flowering plants and cut flowers are, as pointed out above, generally sold direct to the consumer. Where a grower is so located as to be unable to dispose of his stock in this way, he ships direct to a commission house or to the retail florist. If to a commission house, the stock is then sold to the retail florists for what it will bring and a commission charge of 15 per cent made for flowers and 20 per cent for plants on gross receipts. All accounts are settled monthly.

A type of such houses would be a large retail florist, who either grows no flowers or plants or has to make large purchases of stock during the season to help out his own supply. In such cases the grower or his agent generally visits the store of the retailer and takes orders in advance for stock or orders are sent by mail or telephone to the grower. On receipt of cut flowers they are unpacked and placed in large vases containing water, placed in a refrigerator or cold-storage room, where a suitable temperature can be maintained. After the flowers are sufficiently developed they are then offered for sale. There is no large organization required to handle this business, except clerks, decorators, and delivery wagons.

A commission house which deals in cut flowers is fitted with large refrigerators or cold-storage rooms, in which to place the flowers when received from the grower in order to keep them in good condition as long as possible. On receipt of stock from the grower he is credited with the number and kind, and when sold is sent a memorandum showing the total gross receipts and the commission charged. Accounts are settled monthly or semimonthly, as desired.

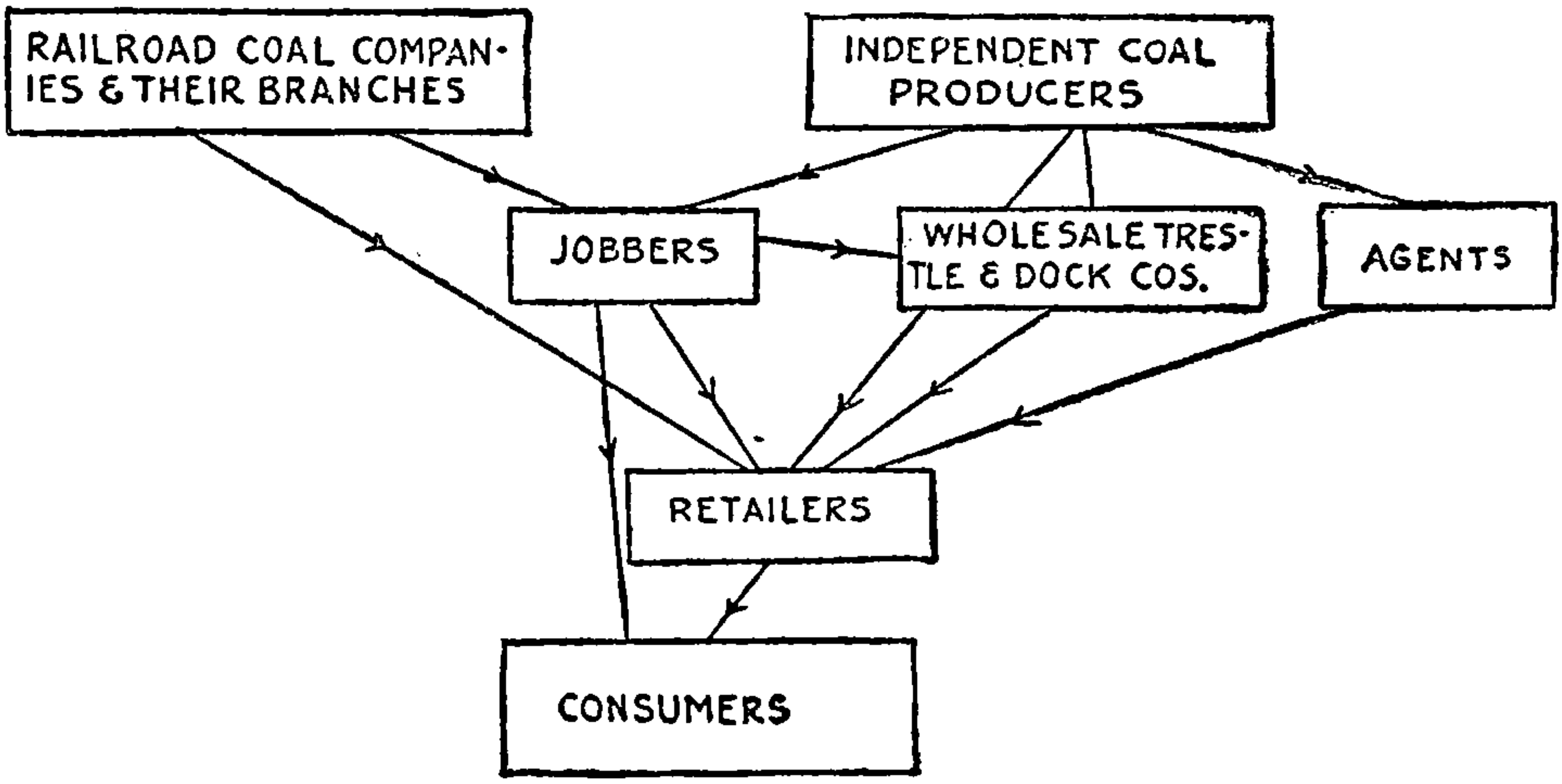
Many commission houses have branch stores in other cities and can reship stock to such places where a shortage occurs. In dealing with cut flowers, however, it is very risky to reship, owing to their extremely perishable nature. In fact, the perishable nature of the stock is such that it cannot be shipped long distances and arrive in condition to be used or to compete with stock grown in the neighborhood. The ordinary florist flowers that are most commonly used would be almost worthless if in transit more than two days.

Very rarely are cut flowers or flowering plants sold at auction.

In all cities having public markets flowers are sold by many of the growers from their own stands direct to the consumer.

Season for cut flowers and flowering plants lasts all year, but sales are heaviest from October to the end of April.[10]

**69. Typical Organization Charts.**—The following diagram shows the trade organization that has developed to handle the marketing of coal. This shows that there is not a very complex and intricate system of distributing coal, as in the case of wheat. No doubt this is one factor that will make the Government control of the industry from the point of view of marketing much easier than otherwise. Also it must be stated that this scheme of distribution is the one that existed before the fall of 1917. Some of the changes brought about and some of the new problems facing these middlemen due to the control of the coal industry by the United States Government will be discussed shortly.


RAILROAD COAL COMPANIES & THEIR BRANCHES
INDEPENDENT COAL PRODUCERS
JOBBERS
WHOLESALE TRESTLE & DOCK COS.
AGENTS
RETAILERS
CONSUMERS

MARKET ORGANIZATION CHART FOR BITUMINOUS COAL

The chart on page 82 shows the main trade routes of pig iron. This is an intermediate stage in a larger process, but it reveals this section clearly. The ore starts from the mine and reaches its consumer, the foundryman, by one or the other of two main highways. Considering the basic character of the commodity, the simplicity of the organization is remarkable. An explanation should be sought.

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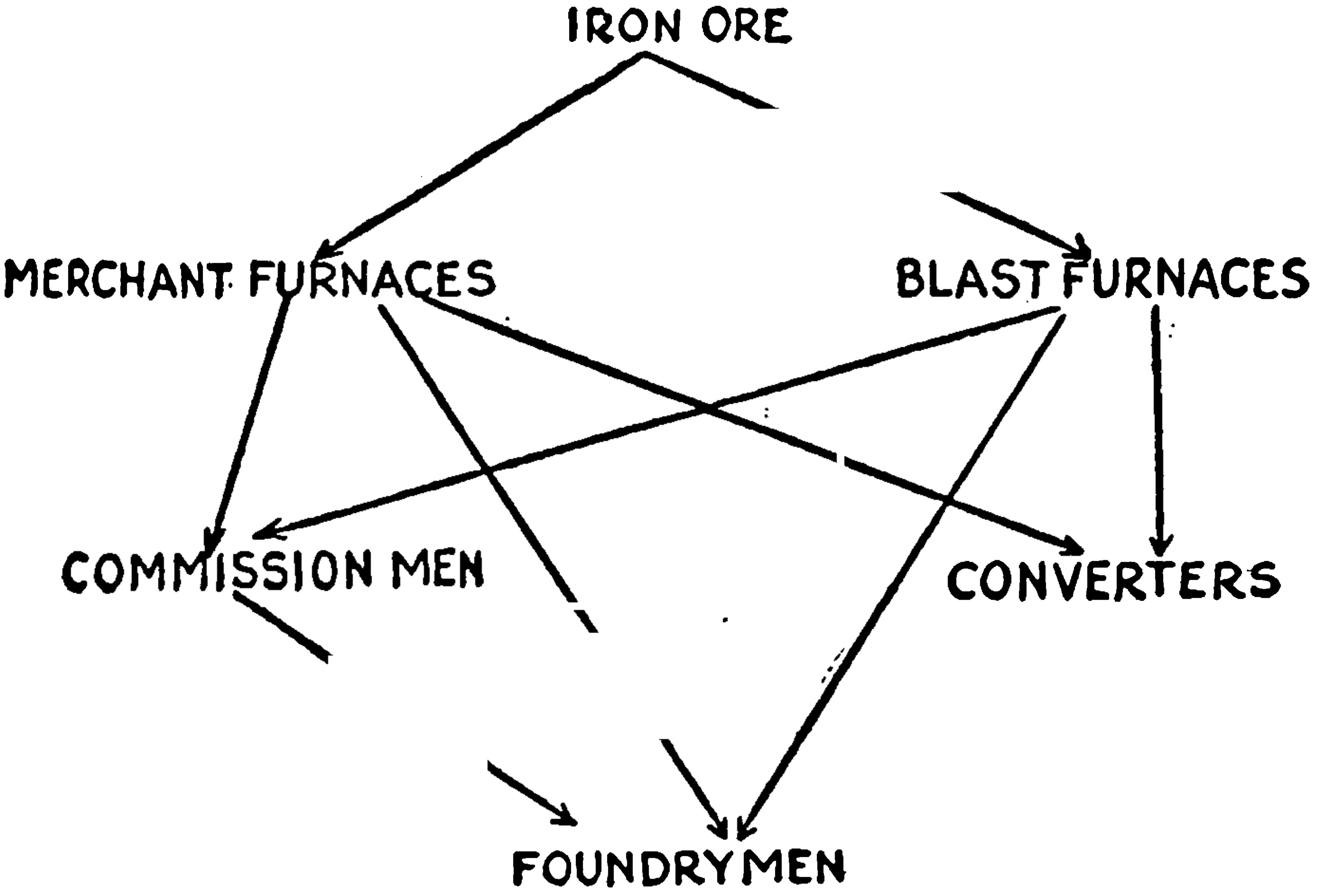
[10] *Ibid.*, pp. 50-52.

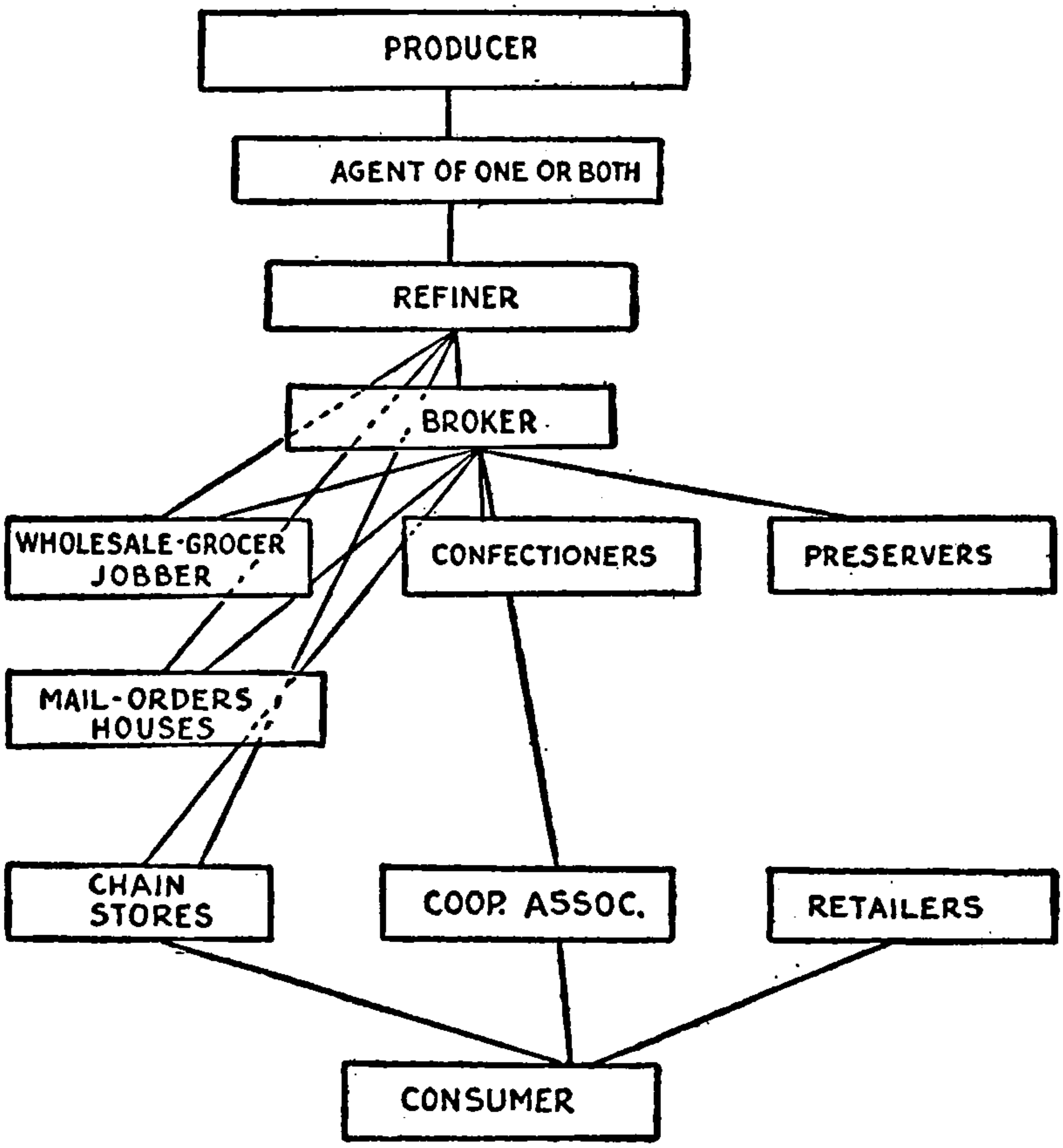


MARKET ORGANIZATION CHART FOR PIG IRON

Further examples of typical organization charts, for sugar and antimony, are given below.

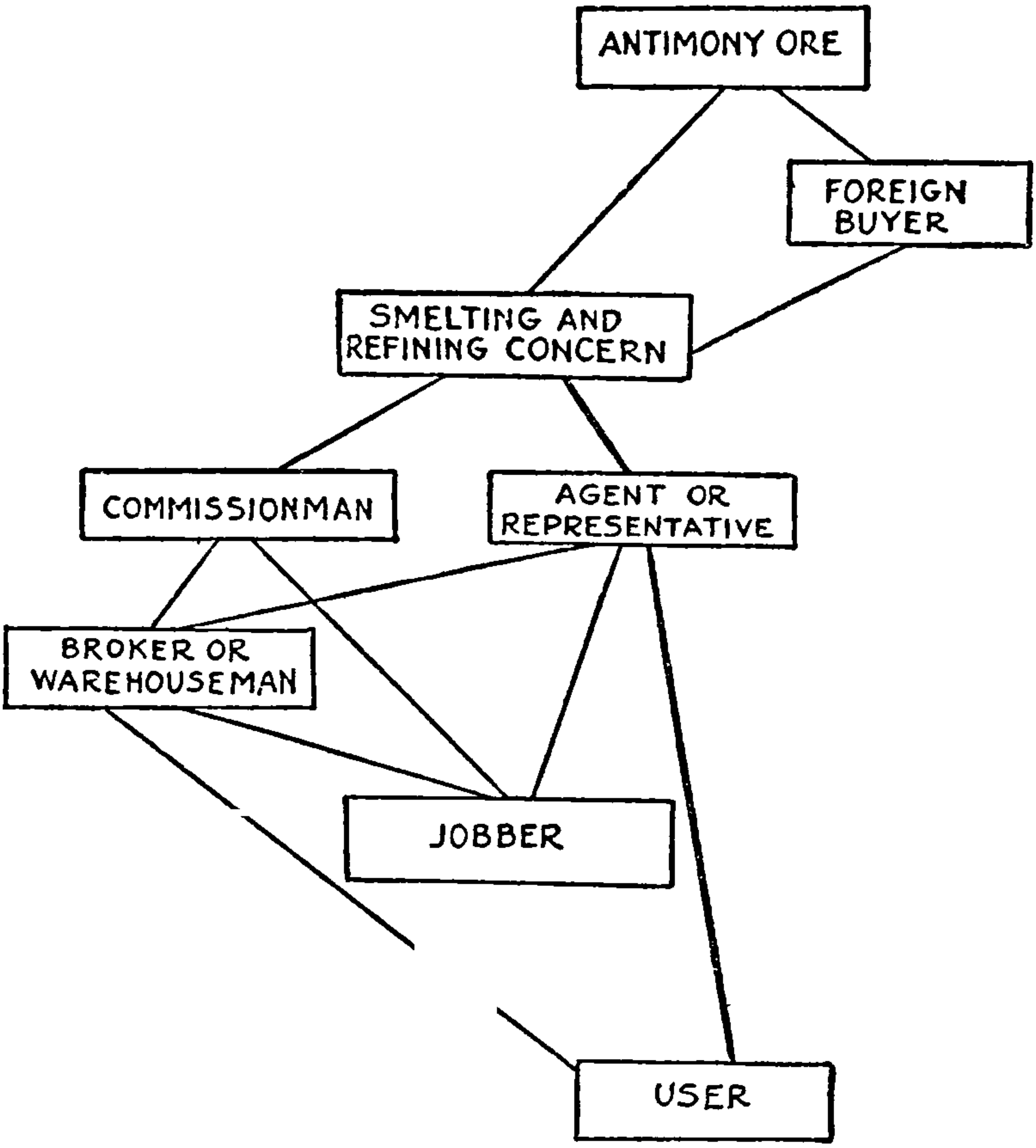
**70. Flexibility of Trade Organization.**—It has been stated that no trade organization is fixed or stable for long. The movement in recent years to "eliminate the middleman," *i.e.,* to combine the distributive functions, has made material modifications. In certain cases the producers have slipped past all the middlemen and sold direct to the consumers. This is illustrated by the selling of eggs, potatoes, and other vegetables by the parcel post. Coöperative societies have in some cases taken over the distributive functions. The Bureau of Markets in the Department of Agriculture has devoted its major efforts toward coöperative marketing. Wholesalers and jobbers have in other cases incorporated the productive functions. This is true of certain canned-food jobbers.

No trade organization can remain fixed. There are too many keen, active minds in business seeking eagerly for better methods. Even where concentration and consolidation have gone far toward integrating the entire productive and distributive process, there is the ever-present potential competition that may quickly beat its way through a more effective path to market. Out of this struggle for more efficient distributive methods comes business progress.


PRODUCER
AGENT OF ONE OR BOTH
REFINER
BROKER
WHOLESALE-GROCER JOBBER
CONFECTIONERS
PRESERVERS
MAIL-ORDERS HOUSES
CHAIN STORES
COOP. ASSOC.
RETAILERS
CONSUMER

MARKET ORGANIZATION CHART FOR CANE SUGAR

There is in business, nevertheless, a strong conservative element. Business practice soon crystallizes into business tradition. Remnants still remain of outgrown methods. The toning up which the mail-order houses and the chain stores have given to the country retail trade is convincing evidence that stagnation was there. This upward climb to better business methods, though slow and painful, is sure and relentless. The present day is witnessing the application of "big business" methods to the distributive process, just as they were applied to the productive process from 1898 to 1902. What far-reaching effects the use of the recently developed trade acceptance may have cannot now be determined. The building of a great municipal warehouse, as at New Orleans, equipped with modern docking facilities and a municipally-owned switch track, will affect the trade organization of those commodities which pass through it. Everywhere in the trade organization, there is this conservatism and this progressivism.


ANTIMONY ORE
FOREIGN BUYER
SMELTING AND REFINING CONCERN
COMMISSIONMAN
AGENT OR REPRESENTATIVE
BROKER OR WAREHOUSEMAN
JOBBER
USER

MARKET ORGANIZATION CHART FOR ANTIMONY

**71. Conclusion.**—A trade organization is, then, the mechanism, or device, for carrying goods to market. It is made up of middlemen who perform certain distributive functions, operating through institutions. These distributive functions may not, in certain cases, be distinguishable, but in the marketing of raw materials and finished products they are isolated sufficiently to make an approach to a study of marketing methods and problems feasible through them. Each commodity may have its own individual distributive problems, but the broad, underlying problems are the same and may be generalized. The existing trade organization is in no case the best or the worst possible one. It is a dynamic thing, changing through the years, ofttimes combining and recombining the functions, but always seeking a better way.

### SUGGESTIONS FOR STUDY

The student should write a descriptive analysis of the trade organization for his selected commodity. There should be included a chart of this organization and a discussion of the strategic points in it. The following are general topics for suggested study:

1. The effect of the character of the commodity and the character of the market upon the trade organization of: (*a*) wheat; (*b*) cotton; (*c*) livestock; (*d*) petroleum; (*e*) wool; (*f*) iron and steel; (*g*) perishable fruit.
2. Specialization of distributive functions.
3. The combination of distributive functions.
4. The combination of the middlemen.
5. The clash of interests in the distributive process.
6. The changing character of trade organization.
7. Strategic points in marketing.
8. Social control of trade organization.

READINGS:

Holmes, G. K., "Systems of Marketing Farm Products, etc.," U. S. Department of Agriculture. Report No. 98.
Weld, *Marketing of Farm Products.*
Huebner, *Agricultural Commerce.*
Westerfield, *The Middleman in English Business.*
Swift & Company, "Marketing Meat Products."
Cherington, *The Wool Industry,* Chap. IV.
Wright, *Wool Growing and the Tariff,* Chaps. VII, VIII.

## CHAPTER V

### THE MIDDLEMAN

**72. Who the Middleman Is.**—A middleman is one who performs some kind of distributive function. "Middlemen are understood to include the series of traders through whose hands commodities pass on their way from maker or producer to the consumer."[1] It is often true that a single middleman combines within himself several functions; a wholesaler may do some retail business, a retailer some wholesale business. The group of economic functions involved in distribution may become centered in a single organization, such as a coöperative society. The very fact that the economic process is a continuous one, that there are no clear lines of division between the actual operation of many of these functions, that two or more are often in progress at the same time, tends to make them coalesce.

There is, nevertheless, a sufficiently clear distinction in the popular mind between producers, middlemen, and consumers, so that certain middlemen may be discussed in connection with their services. Something will be said here about: (1) the development of middleman functions; (2) the buyers and sellers in the local markets; (3) the buyers and sellers in the wholesale trade; (4) the retail trade; (5) the tendency to eliminate the middleman by integration, direct selling, coöperative organization, parcel post; (6) the outstanding problems connected with the handling of raw materials and finished products. The point of view will be that of a descriptive analysis, *i.e.*, an attempt through a brief description to reach certain broad conclusions.

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[1] Westerfield, *The Middleman in English Business*, p. 119

**73. Development of Middleman Functions.**—American industrial and commercial institutions are British in origin; early American trade and industry were simply British trade and industry transplanted. What American business is to-day is that transplanted British industry modified, developed, elaborated by the enterprise, the daring and business intelligence of American business men. The origin of the American middleman was, therefore, in England.

In England, the middleman developed during the years 1660 to 1760. This was a golden age in British business prior to the marvelous development which resulted from the Industrial Revolution. There was a tremendous increase in production and in trade, domestic and foreign; there was the development of machine industry; there was a breaking up and an isolating of economic functions; there was a growing complexity in trade. New ways to market were opened up and commercial areas broadened. Roads and vehicles were improved. Governmental policy was liberalized and some encouragement was given to merchants. There was an increase in population, the number of inhabitants increasing in England and Wales from five and a half to seven millions between 1660 and 1760. This was the period during which England laid the foundation of her commercial supremacy.

To this period of change has been attributed the rise of the middleman in English commerce.

> It is believed that commerce and its growth are inexplicable if little or no countenance is paid to this active, thinking, constructive, organizing class. The class did not exist, except in embryo, in the mediæval system of barter market Before the Industrial Revolution an orthodox system of middlemen had been an established fact, and the modern integrated business is just now beginning to divest itself, in some parts, of its hold. It is important

to discover what were the activities of these new men, what were their relations to each other and to the producers and consumers, what were their functions in commerce, and what their connections with statesmen, national policy, and social life.[2]

The so-called middleman is the merchant, the man who stands between the producer and the consumer. Considered for long as unproductive, the middleman won for himself the recognition of doing a task worth while. As a matter of fact he has performed a great social service. It is to his enterprise, his initiative, his daring and courage that English wares entered foreign markets and multiplied in the home markets. As itinerant peddler, as merchant prince, as specialized salesmen in established markets, the merchant class reached a position of importance where the producing class was almost wholly dependent upon it. In questions of finance, in taking risks, in developing insurance, in finding new markets, in educating the consumers to new wants, it was the merchant class that led the way. "Before the Industrial Revolution especially, the hand that turned the wheel of commerce was not the producing craftsman but the merchant and tradesman."

The middleman had a struggle to justify his existence, for every change in business organization is resisted. It was claimed that the distributive functions were being and could continue to be performed by the guilds or by the church. Besides, it was said, the man who is occupied merely in handling goods, in distributing "back and forth . . . the product of Husbandry and Manufacture" is, like money, unproductive. The concept of time and place utilities had not yet arisen. As a matter of fact, it was not this concept that secured an acceptance of the middleman, but rather the development of the "make work" theory, namely, that a continued subdivision of labor made more work and kept more people busy, by which means alone a nation grew in wealth.

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[2] *Ibid.*, p. 124.

Until the introduction of machinery made possible large scale production, the multiplication of small producing units and the extending markets multiplied the number of middlemen. More and more this group of intermediaries separated the producers from the body of consumers. "The introduction of the middleman into economic life had a most profound influence in the social history of mankind. Instead of local self-sufficiency and separation, a broad economic interdependence and community of interests arose. A competitive system supplanted the mediæval direct-exchange, public-market, fixed-and-just-price system. Supplies were equalized in times and places, and made less dependent upon the accidents of weather. Economic life acquired a speculative quality. The modern categories of economics arose. Business was born."[3]

The modern commercial organization has by no means shaken off the power of the middlemen. They have continued largely because they perform a necessary service, and partly because of the inertia of business. There can be no question, however, but that they would long since have practically disappeared, if they were not really functioning economically. "A profound law governs the processes of civilization. The law is that the civilized man always tends to minimize the variable elements, or the risks of his business, and to depend more and more largely upon the use of clearly defined and intelligible means, the result of his own observation and of the widening experience of the race."[4]

It is this active observation, this keen interest to find the most direct and effective method, that has been the mainspring of development. Besides, business methods have always been put to a relentless test. "The commercial considerations limiting specialization are much more numerous and important than the mechanical. The ultimate appeal in all these matters is to the arbitrament of competition."[5]

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[3] *Ibid.*, p. 130.

[4] C. F. Dole, *Atlantic Monthly*, vol. c, pp. 813-818.

Middlemen, like economic institutions, rise to meet a need. In general, their services are most needed in a widely-dispersed industry, with little local specialization, in which the means of communication and transportation are poor, and there is seasonal activity. Under such circumstances there are small lots at both ends of the process; commodities are collected from many small sources and are distributed to many small consumers. There is then the anonymous producer and the anonymous consumer. The middlemen monopolize the knowledge of supply and the knowledge of demand. Risk and control are theirs. And theirs, too, is the chance to capitalize their superior knowledge of supply and demand.

The development of commerce and trade after the break-up of the manors and the rise of the towns, by means of markets and fairs, is familiar to all students of the history of commerce. The two principles which directed, more or less consciously, the lines of development, have been stated thus: "That, as far as at all possible, sales must be public and at first hand, and that everything which can be produced within the town itself shall be produced there."[6]

This principle of self-sufficiency led to a condition where all the supplies possible for the town market were drawn from its tributary territory, while at the same time, "town handicraft [manufactured goods] had an exclusive right of sale on the market." Thus, it came about that "the territory from which supplies were drawn for the town market, and that to which it furnished commodities, was identical.'" The city dweller and the peasant thus stood in relationship of mutual customers.[7]

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[5] *Engineering Magazine*, vol. xx, p. 709.

[6] Bücher, *Industrial Evolution*, p. 116.

At an early stage, however, the "foreign seller," from another town, found a market for his products when there was no home producer. With his advent the town markets began to overlap and market competition was possible. The distributive system thereupon grew more complex and intermediaries, that is, middlemen, multiplied. "It was the duty of these intermediaries to bring buyer and seller together, to assist in fixing price, to test the goods for possible defects, to select for the purchaser the quantity he had bought, and to see to its proper delivery."[8]

These men were forbidden, at first, to trade for themselves, as is true to-day on the Chicago Board of Trade, but it was probable that retailers existed from a very early time, such as grocers, peddlers, and cloth dealers. What might be called the wholesale trade was exclusively itinerant and market- and fair-trade.

It is clear to see that this was the basis upon which our present commercial organization was founded. In the early Colonial days, in New England, the subdivision of distributive function had not gone far. Boston had its fairs and markets and the state by law established certain marketing periods. There was the period, too, of the tin peddler, the itinerant shoemaker, the meat peddler, and those who carried packs of various commodities from farmstead to farmstead. From this simple system, with extending markets, there has grown a vast, complex structure of distributive machinery.[9]

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[7] *Ibid.*, pp. 114-126.

[8] *Ibid.*, p. 126.

[9] For historical sketch of market development, see Hobson, *Evolution of Modern Capitalism*, Chap. VI; Smith, *Industrial and Commercial Geography*, pp. 850-876; Sparling, *Business Organization*, Chap. VIII; Bücher, *Industrial Evolution*, pp. 114; Day, *History*

Probably the most important point to note in the development of middleman functions is the change from a personal to a wholesale market. The results of this drift from one kind of marketing to another were profound: (1) There was a loss of personal contact; (2) there were then anonymous goods on the market; (3) there was a shift from service to quality and price in selling; and (4) there arose competition between merchants.

The essential features of the American distributive system have been described as follows:

> 1. The necessary outgrowth of the fundamental division of labor between town and country in our national development.
> 2. A development out of the constantly widening distance between the areas of surplus production and the centers of consumption arising from the territorial expansion of the United States.
> 3. The distribution of the excess or surplus farm products among the deficit nations of the earth—that is, the distribution of that portion not required for domestic consumption—involves so many elements of risk to capital and labor as to make this world-wide service to society a distinctively speculative business, of an altogether too hazardous character for producers or consumers to render without subjecting society to still greater risks of providing a regular food supply.
> 4. To develop a new division of labor—that of the capitalist-speculator, whose function it is to relieve both producer and consumer of the hazards of distribution, so that the surplus on one portion of the earth may regularly be supplied to the deficient portion at such a price as will in the long run a little more than balance the gains and losses of this species of commercial enterprise without unduly enhancing the cost to the consumer or unduly depressing the margin of profit to the producer.[10]

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*of Commerce,* Chaps. V, VI; Green, *Town Life in 15th Century,* 2 vols.; Traill, *Social England,* vol. i; Weeden, *Economic and Social History of New England,* 2 vols.

[10] Report of Industrial Commission, 1900, vol. vi, p. 23.

Working through the distributive system as it stands to-day, complex and cumbersome in certain instances, simple and direct in others, a series of middlemen are carrying the raw materials and foodstuffs to market. It is now proposed to discuss the activities of these intermediaries critically.

**74. Buyers and Sellers in the Local Market.**—If the definition of a local market depends upon its geographical proximity to the source of supply, it must be clearly understood that two kinds of processes are at work. In one case, the raw materials and foodstuffs enter these local markets for immediate or at least for local use. In the other case these materials are on the first leg of their journey to primary and terminal markets. In both cases the purchaser may be called the local buyer.

The local buyer is the first, or original, purchaser from the producer. This original purchaser may be the agent of an outside buyer or an independent dealer. In the former capacity he is beginning the process of concentrating materials into large lots; in the latter case, he may be buying for the local market, that is, he may be a local merchant, or he may be acting independently, buying on his own account to ship to the wholesale market. He may go to the farm to buy, as is frequently true in the case of eggs, or to the orchard or to cotton plantation. There may be a survival of the ancient system of barter, where the producer exchanges butter, eggs, chickens, wood, cotton, railroad ties, or other commodities for merchandise. In many diverse ways the first sale is made, and raw materials and foodstuffs start on their way to the consumer.

It has been said of the marketing of the products of the farm that

> there are five ways in which a farmer may market his products, as follows:

1. By direct sale to consumer.
    (*a*) By going direct to residences.
    (*b*) Through public or municipal markets.
    (*c*) By parcel post or express.
    (*d*) To local manufacturers.
2. By selling to local stores.
3. By shipping direct to dealers in large cities.
4. By selling to a local buyer.
5. By shipping through a coöperative association.[11]

There are five different methods of handling milk in the local market. First, it may be delivered to the consumer by the dairyman-producer. This type of organization is rather typical of the small town but becomes less important with the increased size. In this case there are no middlemen. The producer and consumer meet. Second, the milk may be shipped from the farm in milk cans to the wholesale dealer within the city. Third, the producer may sell the milk to creameries generally located in small towns or in the country, or to the milk stations. This type of organization belongs particularly to milk substitutes and to the manufacturer of cheese. Fourth, the producer may sell the milk to large bottling plants in the cities. In this type of organization the milk train becomes important, with all the special equipment needed. It is said that by means of the milk train a monopoly was secured over milk in the New England district. Fifth, the producer may sell the milk to country bottling plants. This is in reality a modification of number four, because it simply means that the dealer has transplanted the pasteurization and bottling process from the city to the country.

There are three ways of marketing bituminous coal in the local market. First, it may be sold direct to retailers, through the selling department or outside agents of the mine operators. Second, it may be sold through jobbers.

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[11] Weld, *Marketing Farm Products,* p. 24.

Or, third, it may be sold to the "wholesale trestle and dock companies." Between 80 and 90 per cent of the entire output of pig iron is used by the steel plant producing it. The rest is sold by merchant furnaces into the general market. There are no local dealers in the handling of anthracite coal at the mines. It is controlled by producers until it reaches the consumer through their own agents or is placed in the hands of commission agencies. Sugar is sold on plantations to refiners' agents. Salt is brought by producers from the mines to distributive warehouses, to be sold to dealers. Peanuts are sold to farmer buyers, who purchase from their neighbors in lots of from one bag up to one hundred, or to the agents of cleaners, or to local warehouses or to commission men or brokers in the wholesale market.

Whatever the channel of trade, and the methods are very diverse, the transaction is the first step from producer to consumer. When the volume of trade warrants it, the wholesale dealer or manufacturer is likely to send his agents into the local market. When control of supply is possible, the producer will tend to control the commodities until they reach the wholesale market at least. But the kind of buyers and the character of the transaction will be adapted to the character of the commodity and the character of the market for it.

**75. Buyers and Sellers in the Wholesale Trade.**—The wholesaler is one who handles commodities in large lots, say, in carload, boatload, or truckload lots. By himself or through his agents he reaches out to touch the producer; he draws from many small sources into the reservoir of his storehouse. He buys in small lots to sell in large lots. In doing so, he is a collector, grader, standardizer, storer, packer. In this process he is also a risk taker. He buys and sells upon his superior knowledge of demand and supply. It is often necessary for him to finance the transaction before it takes place. In general, he must have a knowledge of the commodity, of the supply and demand; he must have capital; he must have a storehouse. He is the buffer between production and consumption; he levels out the seasonal supply geographically and chronologically.

On the basis of the nature of sales made to or through them, middlemen in the wholesale market are called commission men, brokers, jobbers, forwarders, factors, and so forth. These types are by no means distinct, however. A commission merchant, if true to type, never owns the commodities which he handles, but receives a certain percentage of the sale price for his services. This middleman was more prevalent formerly than at present, especially in the marketing of perishable farm products. The broker, if true to type, handles no commodities at all himself, but acts as an intermediary between buyer and seller, charging a fee for his service. The jobber, if true to type, buys goods and sells goods in job lots, or wholesale lots. The real service of a forwarder is to collect from various producers small lots until he accumulates a carload, thus saving in transportation rates. He gets a fee for his services. In foreign trade he may become a broker in space aboard ship or in the car, taking his fee from the transportation company.

The commission merchant needs the equipment required for handling the commodities in which he deals. This may be a warehouse, cold-storage room, coal bins, grain elevators, and so forth. He must also establish the necessary connection both with producers or local dealers, and jobbers or retailers. He must be capable of inspecting, grading, judging what he buys. Nevertheless, the commission merchant, as such, has proved himself an illogical factor in marketing. He has controlled the goods he handled without bearing the risk for them. This situation has given him an opportunity for dishonest dealing, which some did not have the strength of character to resist. He is an example of a middleman who must demonstrate his necessary economic service.

Brokers are middlemen who deal in contracts. They have clients who give them orders to purchase certain goods. Their stock in trade is a superior knowledge of sellers and buyers. As a type they are most familiar, probably, as dealers in stocks and bonds. In the Chicago wheat pit they predominate; in the canning industry there are many brokers. Their fundamental function is to act as sales agent for one party and as purchasing agent for another. As industries increase in size, it becomes profitable for each one to have its own special agent to perform the services of the broker. In a highly organized open market, brokers still have a definite function in buying for and in selling for a distant client. Often the broker takes on other functions, buying outright, for instance, a cargo of coffee or sugar on the sea and then endeavoring to sell it before it reaches port. Or he may sell on commission. It is easy for him to slip over into other fields if he has the equipment to handle the goods. The broker has less control over the commodity than the commission merchant and less risk.

The jobber has been a most potent force in modern business. As a general type he has been alert, aggressive, progressive. Most frequently he has developed from a retailer, having established a successful business and made a wide acquaintance. The jobbers in foodstuffs have "a following of grocers, butchers, marketmen, and other small dealers, many of whose orders are taken in advance and later delivered throughout the city to the purchasers. This class of jobber includes many firms that fill orders for country towns. The order trade is considerable."[12]

They buy outright the materials they handle, and grade, sort, pack, finance them and break them up into small lots or assemble them into large lots. They must be equipped with a storehouse and facilities for handling the goods. Often the big jobbers become producers and retailers as well. In many lines of business they have proved that they do their service more economically than the individual business can do it. The individual business may develop, however, until it can afford to incorporate these functions. "The banker is the middleman—the jobber—of the money market."

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[12] Kiely, "The Middleman in Practice," *Cyclopedia of Agriculture*, p. 241.

The "factor" is a transplanted British business term and is applied most frequently in the United States to a middleman in the handling of cotton. "The planter may consign to a factor, with instructions to hold the cotton for higher prices and then sell it on commission. The factor often makes an advance of possibly two-thirds or three-fourths the value of the cotton, and charges the planter interest on this advance. When the sale is made, the factor deducts his charges from the amount received and remits the net proceeds to the planter."[13]

This is almost an anomalous type, but is most nearly like a commission merchant. He never holds title to the goods; he receives them only on consignment; he stores them; he finances the producers. He sells, like the broker, under orders. With a better warehousing system and more financial independence on the part of the planter, he may tend to disappear.

As has been said, distinction either of functions or of types in the wholesale trade is not clear. A middleman of enterprise and with shrewdness can make a place for himself even against the general tendency. One type of dealer is peculiar to the large milk markets. This is the milk broker. He performs typical broker functions, either finding buyers for the producers or finding producers for the buyers. This work is carried on by a single man or more usually by a corporation. This broker, in addition merely to selling contracts for the delivery of milk, investigates credit conditions and guarantees payment.

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[13] Holmes, *Systems of Marketing Farm Products*, p. 42.

In spite of the wide organization in the iron and steel industry there are pig-iron commission merchants. In the marketing of leather the most important middlemen are the jobber and the finder. The branch warehouse performs the functions of middlemen in distributing salt. The most difficult and technical function for middlemen in handling tea is the blending. Usually the tea jobber blends the tea for his customer. Crushed stone may be handled in carloads by the small country elevator man, along with lumber, coal, and cement, and sold to local buyers by the ton, or by the city yard agent of the crushing company. The outstanding factor in marketing wool is the wholesale wool dealer.

All business institutions are affected by the personality, aggressiveness, and originality of men. Nevertheless, broadly the middlemen types and functions are as indicated above. Broadly, too, the principles involved are as follows:

1. The justification of the middleman is that by his activities certain economies are realized and savings are made equal at least to the returns which he receives.

2. The proof of economical distribution is to be found in the market price. If that price is increased by the intervention of middlemen, there is evidence that they are getting more returns than their service justifies. In theory the test is that many eager minds are seeking the most economical method, and therefore the one existing at any given time must stand the test of active and potential competition.

3. The increasing complexity of the distributive organ-

ization, the increased number of intermediaries, should in reality result in a lowered price, better qualities of goods, better service, that is, increased time and place values, or else the heavy machinery is an incumbrance.

4. In the long run such results as lowered price, a greater diversity of goods, better quality and better service, must be realized or the middleman will be eliminated from trade.

5. The middleman finds his most fruitful field of endeavor where industry is widely dispersed, where there is small unit output, where the means of communication and of transportation are poorly organized, and where production or consumption or both are seasonal in character. Under these circumstances the middlemen are needed to gather goods from many small sources, to store them until there is a demand for them, to transport them for proper distribution both as to time and place in accordance with his superior knowledge of consumer demand.

Because these conditions were fulfilled by the merchants and tradesmen in England, this class grew and thrived in spite of traditional opposition. They proved their worth by their work. That some abused the special privileges that were granted them brought considerable condemnation unjustly upon the entire group. Monopoly of trade at all times will almost inevitably lead to unfair practices. It is to be remembered that foreign trade was concentrated in a few English ports, and in the hands of a few merchants. A port is the neck of the bottle in foreign trade, and whoever controls the facilities and privileges of trade can impose his will upon that trade and secure to himself exorbitant profits. Nevertheless, it remains a fact that the merchant was both necessary and useful.

**76. The Retail Trade.**—The merchant has had a long and varied career.

The history of the concept attaching to the word "merchant" shows that the merchant's relations to the organizations of business varied in the several economic stages in the evolution of commerce. The term has continued in use while its concept varied with time and place. . . . The merchant's business consisted in four branches: (1) buying and selling for himself, or for others on commission, (2) speculating in time and place on merchandise, (3) dealing in money and credit, and (4) insuring goods and ships in transit. Originally the merchants—the Merchant Adventurers—performed all four. By 1760 the merchant might do one, two, three, or four, of these businesses at the same time, as might suit his interests.[14]

Already the functions of the distributors were becoming specialized in England. There was a fairly clear distinction made between the wholesaler and the retailer in domestic trade. The two general movements of goods, namely, the flow from their source towards points of concentration and the flow from these points toward the consumers, could be marked with considerable clearness. A group, known variously as buyers, jobbers, carriers, etc., performed the service of collecting and concentrating the goods. Those who distributed goods to the consumers were shopkeepers, retailers, factors, etc. As is true to-day, some merchants performed both of these general functions, but the distinction was on the whole fairly distinguished.

The character of the function as well as the extent of specialization depended then as now upon conditions and opportunities and capacities. A merchant had to adjust himself to his environment. If the volume of trade was sufficient, one merchant might confine himself to the wholesale business alone. Another would find it necessary to include retailing. A third might be a retailer only. All merchants sought to do what paid them best. This seeking for profit in trade led to a considerable complexity in the distributive organization. The middlemen were no longer a homogeneous type, if indeed they had ever been, but were groups variously employed. Here is obviously the origin of the system that has developed in the United States. The prototype of the vast distributive organization of our own time, the progenitors of all our specialized middlemen, are to be found in the English system.

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[14] Westerfield, *op. cit.*, p. 330.

In the United States the retailer, generally called the merchant, has been expected to carry the goods wanted, at the time and in the quantity desired, and at a reasonable price. When conditions were primitive, he was not supposed to carry fresh strawberries in wintertime, but he was counted upon for bacon, tobacco, sugar, coffee, salt, lard, beans, flour, and many other necessaries, to meet the demands of the community. In the small villages, this retailer, often with the post office in the back of his store, was a considerable figure, and his store was a social center. With changing conditions he has had to meet many new and difficult problems—problems with which he was poorly equipped to cope. Too frequently he was a farmer of scant means and less business capacity, who desired to lead a city life. The high mortality rate is the result.

With the marketing of raw materials, excepting such things as coal, wood, oil, the retailer has had little to do. The mills and factories usually buy in wholesale lots. The retailing of foodstuffs is a most important step in marketing, but in these latter days this function has become so intertwined with the retailing of manufactured goods and the rise of the new types of retailers is so significant that further discussion will be postponed.

**77. Tendency to Eliminate Middlemen.**—It must be remembered that the middleman tends by his own efficiency to eliminate himself, by organizing the market and by making it possible to slip past him. There is also a constant tendency for middlemen who achieve great success to attach new functions. So retailers perform wholesale functions; wholesalers establish retail connections; producers sell direct to retailers or to consumers.

There are four chief ways in which middlemen tend to be eliminated:

*(a) By Integration.*—This is true where the producer absorbs the functions of the distributor. Salt may be carried from the mine to the retailer or sugar from the plantation through the refinery to the retailer, under one management. A ranchman may bring his own stock to market and sell it himself to the packer. The steel manufacturers may reach out to control ore mines, coal mines, ships, railroads, the manufacture of pig iron and of steel. The familiar movement toward integration tends to drive out the middleman as a distinct and independent type.

*(b) By Direct Selling.*—The producer may sell direct to the consumer. This is often the case with truck gardeners, and with other producers for a local market. Frequently a dairyman will work up a milk route of his own in the nearby town. A stockman may butcher and peddle the meat from his own stock. This type of marketing is most likely to develop in the local market or where there is a very large organization.

*(c) By Coöperative Organization.*—Coöperative marketing in the United States has developed most successfully in farm products. Among the best known plans is that of the California Fruit Growers Exchange, wherein the producers of oranges and lemons control the marketing of their products until they reach the retailer or jobber. Many functions of the middleman are thus combined.

*(d) By Parcel Post.*—This is obviously one method of direct selling, but is such an interesting experiment as to deserve separate mention. When the high cost of living began to press more and more heavily on the consumer, the Government undertook the experiment of developing di-

rect contact between producer and consumer by means of the parcel post. There was issued by the Chicago post office, for example, a pamphlet entitled, "From Farm to Table, *via* Parcel Post." This was "compiled and issued by the Chicago post office for the purpose of distribution, in the city of Chicago, to consumers who may desire to purchase butter, eggs, and general produce direct from the farmer, dairyman, or poultry raiser, via United States parcel post." The pamphlet contained a list of producers who had "signified their desire to be listed."

The experiment quickly revealed the functions that had been performed by middlmen. There was the function of financing, of grading, of bearing losses, etc. Business could not develop at long range before confidence between the parties was established.

**78. Outstanding Problems.**—It has already been indicated that the two great, fundamental problems connected with the distribution of raw materials and foodstuffs are risk and control. If control be divorced from risk, there arises an economic anomaly. Commission merchants have suffered from this. Brokers, also, have been able to do business on such a slight basis of capital that men of low standards have crept in. Abuse of their power by unscrupulous men has left a blot on the escutcheon of them all.

There is also the social phase of the distributive problem. By organizing, as retailers, jobbers, brokers, and commission men have done, it may be possible to take advantage of this combined power to secure too large a margin of profit: it may be posible to stifle competition and to level out price.

## SUGGESTIONS FOR STUDY

The student should present a discussion of the types of middlemen who handle the commodity which he is investigating. An organization chart should be made also. The following are general topics suggested for study:

1. Nature of economic functions.
2. Forces tending to multiply the number of middlemen.
3. "Jobbers are essentially speculators."
4. Functional middlemen.
5. Effects of (*a*) character of product, (*b*) character of producing region, (*c*) location and character of markets, upon middlemen functions in marketing cotton, wheat, livestock, petroleum.
6. Make an organization chart to show lines of control in marketing the above products.
7. Describe methods of sale by each type of middleman.

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# CHAPTER VI

## TRANSPORTATION

**79. Transportation as a Commercial Problem.**—"Market competition," said the Interstate Commerce Commission in one of its decisions, "is only an euphemism for railway policy." It is a matter of vital necessity to a railroad that the industries along its lines, the section of the country it serves, and the markets it reaches flourish. Not only has civilization followed the freight car, but commerce and industry also. These are interdependent activities; the railroads cannot live without industry and commerce, and industry and commerce would shrink to dwarfish proportions without the railroads or an adequate substitute.

For long-distance hauls made necessary by broadened commercial areas the transportation function becomes more and more conspicuously essential. This function may be performed by several different means. There are waterways both inland and along the coast; there are the relatively short hauls to the nearby market-place on dirt roads by wagon or truck; there are the more primitive methods of carriage by packs on the backs of men or beasts of burden; there are electric railways for light traffic. In the transportation in this country, however, the steam railroads are the predominant factor. The great bulk of raw materials are carried by them from the mine, the forest or the farm to industrial centers. Semi-finished and finished products are carried from concentration points to places of final consumption or of further fabrication. The industrial centers of New England, the cotton growers of the

South, the fruit growers of the West, the farmers of the Middle West and Northwest are all dependent upon railroad transportation.[1]

This is stating in concrete terms what has previously been shown graphically.[1] Transportation is a pervasive factor, entering into every process of every industry and into every process of distribution. The costs of transportation run against every commodity at every stage of its progress. It is a profound commercial problem.

The carrier function has been recognized for a long time. Only comparatively recently, however, have the economic problems been attacked with seriousness. Many of them have as yet been dealt with only cursorily, such for example as the terminal freight charge and the economic location of transportation lines. The fact is that transportation problems have always kept ahead of those attempting to deal with them, in their increasing complexity and scope. Projected highways have had to struggle with later projected canal systems; canal systems with steam railroads; steam railroads with electric trolley lines, motor trucks, airplanes. And the end is not yet.

The carrier creates both time and place values. For the purpose of creating place values most effectively, the country is to-day enmeshed in a network of roads, canals, trolley lines, and steam railway lines, and ships ply in the coastwise, river, and lake water routes. Commission houses and forwarders, engaged in foreign trade, undertake to carry goods to all important trade centers, and "to all points beyond." Through the development of a worldwide transportation system, the world has become a single great market for certain commodities.

Charges run against goods from the moment they enter the economic process, from origin to consumption, and deterioration is often rapid. The time element, therefore, becomes more and more important. Hence the development of through carload shipments, of fast freight lines, of quick local deliveries by trolley or truck. And that most perishable of all commodities, market information, may find a speedy means of transportation, aside from the telegraph and the telephone, in the airplane. The slow and sluggish barge may bring ore leisurely down the lakes; cotton may be able to spend the necessary days to move coastwise in steamers or even sailing vessels, and coal may spend the summer reaching its destination by boat and slow freight. This is true only because the ship or car is not alone a conveyance but also a warehouse; these goods are being stored while they are being carried.

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[1] See page 3.

It has been estimated recently that the tonnage on the railroads of the United States consists mainly of bulk traffic. Three-fourths of the total tonnage is made up of raw materials and foodstuffs in a proportion about as follows:

| | |
|---|---|
| Minerals | 55.72 per cent |
| Forest products | 11.33 per cent |
| Agricultural products | 8.75 per cent |

About four-fifths of the freight in the United States is carried in bulk, that is, in carloads or trainloads.

The carriage of commodities in this country is for a relatively long distance. Hence there are large cars and long trains. Some years ago the standard capacity of a freight car was 40,000 pounds; now cars of this size make up less than 7 per cent of the total number, and less than 4 per cent of the hauling capacity. These estimates are exclusive of privately-owned cars. Nearly two-thirds of the freight cars are to-day from 60,000 to 80,000 pounds capacity. About 12 per cent have a capacity of 100,000 pounds. In Europe a freight car of 40,000 pounds capacity is among the largest; a "ten-ton truck" is the standard. In England coal, iron ore, and heavy bulk traffic are regularly carried in fifteen- or twenty-ton "wagons"; in France, the "wagons" that would carry "8 *chevaux*" or "40 *hommes*" are a familiar sight. The average freight train load in the United States is about 352 tons, at least three or four times that prevailing in Europe.

The transportation system, like every other industrial and commercial system, develops and adapts itself to meet economic needs. Three important factors that have helped to determine the size of the freight car and the size of the train are the character of the traffic, the length of the haul, and the large-scale business of the country. The traffic in raw materials and foodstuffs is not only of vast amount but also of a greatly varied character; grain, cotton, livestock and meats, fruits, nuts, butter, eggs, poultry, coal, ore, oil are carried in thousands of carloads for hundreds and thousands of miles.

> This summary gives no adequate idea of the actual handling of two million freight cars that are in service day in and day out; of the tens of thousands of freight trains that are moving by day and by night, carrying foodstuffs to markets, materials to mills and factories, and finished products to warehouses and retail dealers. This is the function of the railroad. Upon its successful performance depends the material welfare of the country, and its successful performance in turn rests upon the prompt and efficient conduct of the processes of agriculture, of industry, and commerce.[2]

**80. Transportation to Local Market.**—It is rare indeed to find a situation where there is no haulage from source of material to factory, mill, or consumer. The farmer must haul his crops from field to granary or to the local market; no steel mill has all of its materials at hand; even in a stone quarry there is need of haulage in small trucks or by overhead wire. It may be said that there is a transportation charge of some sort from the point of origin until the commodity in its finished form reaches the consumer.

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[2] McPherson, *Railroad Freight Rates*, p. 13.

Usually the haul to a local market is made by a local conveyance, and usually the producer's. The farm wagon has been most serviceable in this kind of haulage, although in many places now the automobile or truck is displacing the wagon. One company in central Indiana has a fleet of twenty-five trucks for hauling poultry, eggs, and butter. The United States government, through officials in the Department of Agriculture, made some investigations "to determine the feasibility of a national campaign for rural express connecting large cities with nearby producing centers." Coöperative haulage to the local market, as for instance among dairymen, has made possible the use of trucks. The following item is also of interest:

> In Iowa, one hundred and thirty-three miles would be a long distance to drive hogs, or to haul them in a horse-drawn wagon, but a load of 1,230 pounds was carried from Chariton to the packing plant in Ottumwa, bringing the top price because they were in such good condition. If sold at the local market, the price would have been lower, local dealers would have taken their profits, shipped by rail with consequent loss in weight, and the pork chops cost more when sold to the ultimate buyer.[3]

The average distance from plantation to local shipping points for cotton has been reckoned at from seven and nine-tenths to fifteen miles. The average load was a fraction over three bales. The average cost per hundred pounds was from nine to twenty-three cents; per bale about eighty cents. From 555 cotton plantations surveyed to their respective local shipping points, shipment by wagon cost on the average sixteen cents per hundred pounds.

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[3] *Timken Magazine.*

Generally speaking, the initial haulage to the local market is done by the producer and by his own conveyance. But all improvements in vehicles not only widen the horizon of life for the producer but broaden the local market as well. It has been said that the automobile has increased the living radius of the farmer by fifty miles; the local market has expanded proportionately. Usually, too, this item of cost is not isolated.

Some comparative cost figures were made in 1915 to show the relation in expense of local haulage by horse and wagon and by truck.

> These figures show that it costs $4.72 per day to operate a one-horse truck, or $127.02 a month. The cost of up-keep of a two-horse team is $7.44 per day, or $202.04 per month. . . . A horse must be fed, housed, maintained, and cared for during 365 days, but to get his actual earning capacity there should be a deduction of fifty-two Sundays and eight holidays, leaving 305 effective days. A horse's up-keep in idleness is the same as in times of actual service.[4]

The struggle for competency in marketing methods begins thus early, and extends to the end of the process. The horse displaced the human carrier; the truck is driving out the horse and later may likewise yield to a more effective method.

The carrier's functions, even at this early stage, however, are not simple. "The carrier's function is not a single one or a simple one. There are always two phases to his task: he must transport and he must protect; he is a carrier, he is a bailee. From the moment he receives the goods, he is a warehouseman until he delivers them to the receiver."[5]

There have been, and there are, wasteful and inefficient methods in handling as well as in hauling. The wastages in handling grain, cotton, coal, fruit, eggs, and countless more commodities in this initial stage are well known. But the producer, as a carrier, is learning to perform these two functions, of transporting and of protecting, more effectively because he is learning that the risk is his. In transporting to the local market, usually, the producer controls, and the producer bears the risk for his products.

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[4] Trade Journal, January, 1915.

[5] Duncan, "The Uniform Bill of Lading," *Journal of Political Economy*, vol. xxv, p. 691.

**81. Transportation to the Primary Market.**—On the second leg of the journey from producer to consumer, from the local market to the primary market, the dominant means of transportation is the steam railroad. Primary markets are dependent upon railroads for their very existence, especially those inland. It is in the transportation between these markets that the great commodity movements may be seen, the vast ebb and flow of raw materials and foodstuffs, and the "back wash" of manufactured goods.

The functions of the carriers here are the same, although of vaster proportions, as those at the earlier stage. The carrier still must transport and protect. Control may or may not have passed out of the hands of the producer or local buyer, depending upon whether or not he has retained the right to divert the shipment in transit. The risk of loss from mishandling has been shifted to the carrier. Risk for deterioration and for market fluctuation attaches to the buyer or to the seller according to the nature of the sale.

So important have these functions of the carrier become, so vital to the interest of so many people, that the railroads are no longer private enterprises, like other businesses, but quasi-public enterprises, that is, private property devoted to public service. Populations have increased and have become concentrated in large cities on the basis of effective transportation facilities, no less than upon the basis of machine production. Transportation has been called the "basis of civilization." And because the service performed by the carriers is so important, railroad companies have been compelled to take their full share of responsibility, and to submit to state and Federal supervision.

Competition in transportation to the primary market is of three different kinds; (1) competition of routes, (2) competition in facilities, (3) competition of markets. The competition of routes arises wherever "two railways are exposed to identical commercial conditions both at the point of origin and destination."[6] This happens where there are parallel railway lines, where a railway, a trolley, a canal, a river, or even a dirt road afford parallel facilities. The West Shore Railroad and the Nickel Plate route were built to compete in this way with the New York Central Railroad and the Lake Shore Railroad. A similar situation exists between Chicago and St. Louis. From Columbus to Cincinnati one may see not only a rival road, but also a canal, a trolley line, and a dirt road. Such a situation will result in rate competition.

The second type of competition, that of facilities, is one of service. "Such competition is confined safely to rivalry for business at the established rates."[7] The number of trains per day or week, the speed of trains, efficient methods of handling, are all parts of this competition. It is a healthy sort of competition, and makes for continual improvements.

The third type is competition of markets. Not only does the railroad desire to keep every one in business, but also to increase business. A widening market may mean more overlapping of markets and that manufacturers and merchants have more competitors. Furthermore, railroads are not looking for any one kind of traffic, but a satisfactory sum total. There are direct hauls and back hauls; there are single rates and combined rates. "The point to carry forward is that commercial competition demands that in every case not single rates but the sums of all the connecting rates for each competing person or region shall be properly adjusted. If this be not done, some one will be excluded from the market and put out of business."[8]

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[6] W. Z. Ripley, *Railroad Rates and Regulation*, p. 114.

[7] *Ibid.*, p. 116.

These three types of competition appear in their most complex forms in the wholesale trade. Producing centers, market centers, individual business interests, railway interests, are all involved. If a flat rate is given, the railroads can maintain a parity among themselves and shift the rivalry to the middlemen. Often this is not consistent with keeping every one in business. If Chicago has been getting its cement from down state or from Indiana, should the railroads grant to a steel corporation in South Chicago rates to match its proximity to the market? A few cents may divert wheat from Chicago to New Orleans. How shall rates on lumber be adjusted to the receding line of timber supply?

> The intricacy of freight rate adjustment in response to the subtleties of commercial competition depends only in small measure upon the absolute freight rate imposed. The main problem is really that of relativity. But this does not mean mere relativity as between directly competing commodities or places. A strict relativity based upon commercial conditions must often obtain as well between the rates on raw materials and their own finished products; between all the various by-products in an industry; and, of course, always as between goods capable of substitution one for another.[9]

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[8] *Ibid.*, p. 123.

[9] *Ibid.*, p. 134. For detailed discussion of these points see *Ibid.*, pp. 114-46.

Transportation by water has always been a potential, if not an active, factor in the United States. The railroad freight rates from Chicago to New York or to New Orleans, from the cotton-producing regions to New England, from New York to the Pacific coast, are all affected by water carriage. This is particularly true when time is not of the essence, and place values dominate. Ohio has a heavy annual tax for a decrepit canal system. The Erie Canal was improved during the war. Iron ore came by water from mines in Eastern Tennessee to Chicago during the railroad congestion. The agitation of a deep-water way from Chicago to the Gulf and to the Atlantic will not "down." Nevertheless Cincinnati was reduced to a second-rate trading center because she was dependent on water transportation, and St. Louis had to await the development of an adequate railway system.

The water route, in general, is cheaper but slower. For low-grade materials, it can compete with railroads and may serve certain sections not well equipped with other carriers. "Although inland water rates are usually lower than rail rates, there are a few exceptions to this rule. Between Hartford, Connecticut, and New York City, the rates on apples, eggs, hay, and potatoes are the same by rail as by water, although the water route is 52 miles longer than the rail route; the rates per hundred pounds on apples and eggs are higher between Charleston, West Virginia, and Cincinnati by boat than by rail."[10]

It is a delicate matter to tamper with rates to primary markets. A shift of a few cents either way may make or mar a trade center. Transportation is an artificial economic factor that can be used to counteract natural disadvantages for a considerable period. Many industries have been kept going for years after they have ceased to be economical, by a transportation rate. From this aspect, too, transportation is a factor of great commercial importance.

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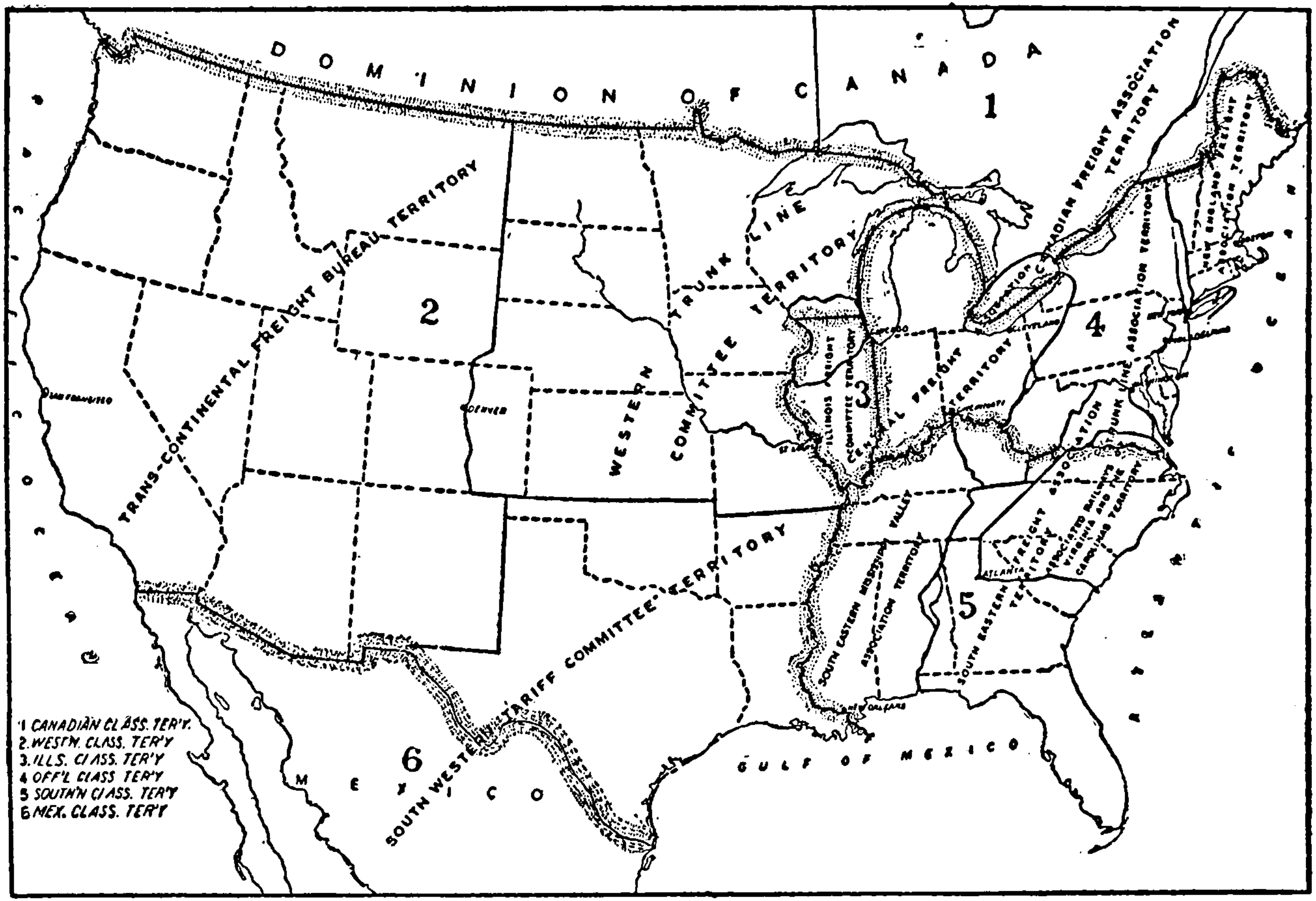
[10] Weld, *Marketing Farm Products*, p. 244. For full discussion see Andrews, U. S. Department of Agriculture, 1914, Bulletin 74, "Inland Boat Service."

**82. Transportation to Terminal Markets.**—There are no new problems raised by transportation from primary to terminal markets. In so far as these latter markets are at the seaboard, carriage by water is of increased importance. On these points, too, there is usually a combined ocean and land rate to a foreign port. Cotton, for instance, will go from any southeastern port to Liverpool at the same rate. All the Gulf ports are likewise on the same basis. Otherwise the carriers perform the same functions for, and are of equal importance to, the terminal markets as the primary markets.

**83. Rate Districts.**—In the effort to make transportation charges that are fair to all interested parties, there have been created certain rate districts or regional rate structures. These regional rate structures have been more or less empirically determined; they have developed without a conscious or careful preplanning. The principal factors in their determination have been, (1) the geographical situation of the region, (2) the natural material resources, (3) the needs of the people and the industries, (4) the general physiographical relation to sources of supply and to markets, (5) the competitive transportation facilities, (6) and a combination of all of these factors in relation to all regions.

The fundamental problem of a transportation system is to develop a region economically. Carriers thrive, if at all, upon an increasing volume of business. In the economic development of a community the necessary length of haul is often the controlling factor. But each region will find it necessary to adjust its own rate schedules to its own par-


DOMINION OF CANADA
1
CANADIAN FREIGHT ASSOCIATION TERRITORY
NEW ENGLAND FREIGHT ASSOCIATION TERRITORY
TRUNK LINE TERRITORY
TRUNK LINE ASSOCIATION TERRITORY
4
CENTRAL FREIGHT ASSOCIATION TERRITORY
3
ILLINOIS FREIGHT COMMITTEE TERRITORY
CENTRAL FREIGHT TERRITORY
WESTERN COMMITTEE
2
TRANS-CONTINENTAL FREIGHT BUREAU TERRITORY
DENVER
SAN FRANCISCO
SOUTH WESTERN TARIFF COMMITTEE TERRITORY
6
MEXICO
VALLEY
SOUTH EASTERN MISSISSIPPI ASSOCIATION TERRITORY
NEW ORLEANS
5
SOUTH EASTERN FREIGHT TERRITORY
ATLANTA
ASSOCIATED RAILWAYS VIRGINIA AND THE CAROLINAS TERRITORY
CHICAGO
CINCINNATI
GULF OF MEXICO
PACIFIC OCEAN
ATLANTIC OCEAN
1 CANADIAN CLASS. TER'Y.
2. WEST'N. CLASS. TER'Y
3. ILLS. CLASS. TER'Y
4 OFF'L CLASS TER'Y
5 SOUTH'N CLASS. TER'Y
6 MEX. CLASS. TER'Y

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MAP OF RAILROAD FREIGHT CLASSIFICATION TERRITORIES AND FREIGHT TRAFFIC ASSOCIATION TERRITORIES ticular needs. This fact is illustrated in the regional rate structures of the country.

There are five of these rate districts throughout the country as shown by the accompanying map. Each region has its own peculiar structure, determined by the factors mentioned above.

84. *New England Rate District.*—The chief industrial and commercial factors underlying the rate structures may be described as follows: the mills and factories of New England must have raw materials, coal, wool, cotton, etc., and the manufactured goods must be able to compete in the markets of the country, if every one is to stay in business. For purchasing raw materials and for selling in "foreign" markets, the manufacturers of this district must be on a substantial equality. In consequence, the tendency is to make a flat rate on raw materials from outside to any point within the region, and to give practically the same rate on manufactured goods to the outside market.

This system tends to equalize all producers within the district so far as transportation is concerned, and to throw the burden of competition back upon efficient methods of manufacturing and selling. Charges must be adapted to meet water rates and will inevitably work to level down advantageous locations. The entire district, also, must be kept in business as compared with adjacent districts.

85. *Trunk Line and Central Traffic District.*—The rate system on commodities east and west between Chicago and St. Louis and the Atlantic ports has been based on the great trunk lines that reached out from New York, Baltimore, and Philadelphia, crossed the Appalachian barrier, spread in a web through the fertile region beyond, and centered first in Chicago and Cincinnati, then continued to the Mississippi River. The rate system used in this district is known as the "percentage system" in which the rate from Chicago to New York, as modified by the possible

water route, is 100 per cent. All other rates are certain percentages of this rate. Each percentage holds for all cities and towns within a zone extending north and south. Cincinnati is 87 per cent; St. Louis is 116 per cent.

This is considered one of the most stable rate systems in the country, and it has been said that a great number of the rates will be definitely established from this basic rate. It may be seen that the rate presupposes a relatively stable industrial and commercial equilibrium. A great, sudden change might disturb the basic rates and demoralize the entire system.

86. *Trans-Mississippi and Trans-Missouri Rate District.*—The railroad web spread out "fan-shape" beyond the Mississippi and Missouri rivers. Many rising towns were clamoring for some rate advantage. It is obvious that there is here no base line for a basic rate as between New York and Chicago. Industrial and commercial conditions were by no means stabilized. The railroads perforce must compromise. The result is a system of "fixed differences," under which certain groups of cities are given the same rate from a base city.

In consequence there has developed a "natural" territory about each trade center where wholesale merchants have an advantage in respect to rates on freight. At the same time a jobber is prevented from driving his competitor in another center out of business. The freight rates tend, therefore, to keep them all in business within certain bounds. Each wholesaler is protected in his own bailiwick.

87. *Southeast Rate District.*—The rate structure in the "Old South" developed long after the chief crop, cotton, had worn a channel to market. As quickly as possible, it sought a water course or a port. The main concentration points were therefore connected with a water route. Upon this as a basis, railroad transportation developed, seeking first to join the interior with a water route. As a result

there arose a system called the basing-point system, where a rate from origin to a basing point was given, and then an additional charge was made back to intervening points and on to nearby points. The water routes are still effective as actual and potential competitors. A flow of food and feedstuffs began before the Civil War from the Middle West; long before cotton and tobacco had been carried North and abroad. Household utensils, tinware and small hardware, fish and bacon made a partial back-haul from the East to the south.

The Civil War cut across inland transportation during the period 1861-1865, but the rate structure has in fact been greatly molded by these channels of trade. Concentration points for cotton will show this fact. "If the basing points be abolished and a scale of rates fixed that uniformly increase with distance, the source of supplies will be driven back to the source of production. The retail dealer will no longer be able to keep as great a variety of merchandise on the same capital, and as he will not be able to so promptly replenish his stock, it will no longer be fresh."[11]

88. *Texas Rate District.*—The State of Texas has tried to build up a rate system all its own. The idea underlying it is that the State should not have one or two large distributing centers, but many small ones scattered throughout the region, each serving its natural territory. The Railroad Commission of the State sets a maximum rate that is to be charged for intrastate traffic. Each trade center can have its freight carried for a rate increasing with the distance away until it reaches the maximum, and then the same rate must be charged to all points beyond. This gives each town an advantage in the territory immediately surrounding it, with a "no man's land" farther out. The system is intensely selfish and short-sighted, for no state

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[11] McPherson, *op. cit.*, p. 89.

can live to itself alone. It is called the common-point system, because from outside, say, from St. Louis, freight pays the same rate to every place in the common-point territory. All trading centers within the territory have, therefore, an equal opportunity so far as freight rates are concerned to become the jobbing center. A glance at the map will show the effect of the system.

89. *Pacific Coast and Transcontinental.*—The principle on which rates to and from the Pacific Coast have been made is thus stated by McPherson:[12] "The problem of the railroads serving the Pacific Coast is, therefore, to provide that adjustment of outbound rates which will stimulate the consumption of her products, and of inbound rates that will bring to her people the commodities which they require without undue enhancement of the price." Many factors enter here, such as, water routes, Canadian roads, competition between the East and the Middle West. Rates are "blanketed" back from the coast to meet water rates; they tend toward a postage-stamp rate from Chicago eastward to keep an equilibrium. When traffic comes eastward, it is found that oranges have a rate of $1.15 per 100 pounds from the packing houses of California to every point east of Denver, and lemons are fifteen cents per 100 pounds less to meet the competition from Sicily.

**90. Classification Rates.**—On the basis of these rate districts commodities are classified by qualified and authorized associations. The same rate applies to all commodities of a given class. Thus, the rate fixing is greatly simplified and there is a commendable tendency toward standardization. It is a long, slow process, however, to secure uniformity of action even in regard to bills of lading where uniformity is so obviously desirable. There are the Official Classification, the Southern Classification, the Western

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[12] *Ibid.*, p. 104.

Classification, and the Transcontinental Classification systems.

With widened markets there is more and more traffic between these rate districts. These boundaries are therefore of less and less significance. Broader forces are at work upon the rates than those within the region. These forces are national or even international in character. The qualities of a commodity that affect transportation in one section will similarly affect it in another. If the same rate principle is applied there is a tendency toward a leveling out. The movement for uniform classification has, however, always met with obstacles. In this opposition business tradition has been a strong factor.

**91. Commodity Rates.**—The four classifications indicated above will take care of 21,700 or more articles. Their purpose, as stated, is simplicity. In 1896 there were 131,597 different schedules; in 1911, there were 93,821. But many commodities are taken out of classes and given special rates. The reasons for these commodity rates are: (1) a recognition of market competition; (2) the result of the efforts of some particular lines to secure advantage for some particular shipping point; (3) continuance of special rates which were formerly received in the way of rebates; (4) to assist particular industries in marketing products; (5) coöperation in building up a new industry; (6) influence of large shippers in routing traffic; (7) to provide combinations not found in classes; (8) large shipments for long distances; (9) for commodities of low grade such as sand, gravel, paving blocks, cement, crushed stone; (10) special market conditions.

The principle of commodity rates has been stated by Professor Ripley as follows: "No single tariff is applicable to any large number of commodities. Each one must be regarded as a law unto itself. Not only does the ultimate amount which each is able to bear depend upon the value of that commodity but also the conditions determining competition with respect to it must be different all along the line.''

Commodity rates are illustrated by the great staples of the country, such as grain, cotton, coal, wool. In regard to these commodities the following cases appear:

1. Commodities which have widely-extended productive areas and widely-extended consumptive areas. The situation is illustrated by grain, grain products, livestock, and dressed meats. Rate solution here has come through an equalization by way of different gateways, *i.e.*, primary markets. The aim of such rate making is to keep all aggregates the same from the entire region of production.

2. Commodities with a widely-extended area of production with converging lines of transportation to places of final manufacture, which are few in number, and are confined in area. Illustrations of this situation are wool and bullion. The rate solution here is to maintain an equilibrium between places of production within the whole area of production.

3. Commodities with widely divergent sources of supply and common markets, such as fruit and vegetables from the West and South, destined for markets in New York, Chicago, and New England. Rate solution here is an equalization of charge, regardless of distance.

4. Commodities with one limited source of production and a far-flung market, such as petroleum, ore, Sea-Island cotton. The competition here is on substitute commodities; the price, including freight to all points, is thus limited.

Fully 75 per cent of traffic in the United States is carried on commodity rates. The tendency should be for business to become more and more stabilized, and for more and more commodities to fall into classes. A more scientific and thoroughgoing classification would greatly help.

**92. Terminal Charges.**—The charges against commodities within the market centers are out of all proportion to railroad charges. It has been said that terminal costs absorb about 80 per cent of the total rate. Switching cost in Chicago has equalled and sometimes exceeded the total amount which the railroad received for carrying freight. The handling in Chicago of goods in less than carload lots from Pittsburgh to Milwaukee has cost more than the entire freight. This situation has resulted from the fact that railroad rates have not taken into account the increasing terminal costs and charges.

Delivery and transfer charges are relatively high everywhere. It was estimated during the war by the Commercial Economy Board that 100,000 men and millions of dollars in equipment could be used for war service, if delivery was cut to one per day.

> Secretary Redfield has estimated that the factors of distribution represented by the word cartage are more costly than the total railway freight rates of the country involved. Take a typical example: Four glass tumblers at four cents each were packed in excelsior and delivered in a basket worth 50 cents. The driver made a second trip to get the basket. Thus the cost of packing and delivering cost the store far more than the value of the goods, which could have been carried home by the customer. . . . Deliveries by retail stores, which average a cost of about 3 per cent of net sales, should be reduced to one a day.[13]

Where freight stations are not centralized or economically located, where the drayage business is closely organized, the expense of terminals is heavy. It is an absurdity that commodities can be carried hundreds of miles at a less charge than is required to get them from the freight house to their local destination.

**93. Special Cars.**—To meet the needs of transportation, various kinds of special cars have been built. In 1913, there were 2,445,508 cars of all kinds. Of these 51,700 were passenger service cars, 2,273,564 were freight cars. The type of car capable of most all-round service is the box car, of which there were 1,032,737 in 1913. The flat cars numbered 147,604.

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[13] *New York Times,* January 22, 1917.

The real problem in this connection has arisen in regard to special types, or limited-service cars. There are stock cars, coal cars, tank cars, refrigerator cars, and express cars. There were, in 1913, 78,308 stock cars, 871,379 coal cars, 8,216 tank cars, 43,389 refrigerator cars, and 12,943 baggage, express, and postal cars. Special, or limited-service, cars have been built by private companies more extensively in some lines than by the railroads. The refrigerator car is an example. So strategic and revolutionary was this type of car in the meat-packing industry and later in the carrying of fruits, melons, and vegetables, that private control of them gave an undue advantage in competition.

The problem of private or divided control of special cars in this country, as is true of all freight cars in England, is not yet settled. The railroad companies have claimed that they could not afford this extra equipment since it was not possible to utilize it all the year around on each system. To make these cars pay, it was said, they must be shifted from one part of the country to another, like shock troops, to meet the seasonal crop emergencies. An independent ownership might accomplish this; a single railroad cannot. A central car association has, therefore, been proposed. What happens in this regard is of extreme importance to merchants and manufacturers.

**94. Car Supply and Routing.**—The efficiency of freight railway service is tested by its ability to meet the demands in every part of the country when they arise. There are seasonal demands and emergency demands to be met. The orange and the lemon crop in the West and South; the melon crop in Indiana, Colorado, and the South; the wheat crop; the shipment of cattle, coal, cotton, corn, from source to market; the tons of ore; the great flood of manufactured goods—all must be cared for with justice to all producers and all consumers. The equipment must be able to carry the peak of the load. Inevitably there will be idle cars here and there; some caught in an eddy of the trade flow, some waiting for the seasonal demand. There must be a reserve.

Between July 6 and December 26, 1919, 76 per cent of the entire wheat crop was moved from the farms; in amount, 645,318,000 bushels. This is a tremendous drain on the freight-car supply, when there is a demand for the movement of many other things at the same time. The strawberry crop may become ripe suddenly; the cantaloupes may be ready to pour out in a great flood. These things will not wait without loss. Freight cars must be at hand to carry them. To meet these ever recurring and insistent seasonal demands the cars must be so routed as to converge at the proper spots. For this purpose, government reports must be studied to find out estimated volume and effects of weather on ripening conditions.

Emergency demands also arise. The summer of 1917 was unfavorable in the Northwest and in Texas. When winter came on thousands of cattle faced starvation, or the market in a thin, emaciated condition. In the Middle West, however, there was ample supply of foodstuffs. Stock cars had to be rushed at this unusual period to carry the cattle from the drought-stricken regions to the regions of plenty. During the same year the potato crop was threatened with destruction by early freezing weather; cars had to be assembled to carry this crop. In the autumn of 1919 the railroads built up a movement of coal from 11,000,000 tons weekly in September to 13,000,000 in October, a greater average than for any previous period.

These divergent and often antagonistic demands make the problem of routing cars not only most important but also exceedingly difficult. Previous to the war there had existed a great economic waste in roundabout routing. There was circuitous rail carriage and carriage over undue distances. The result was "diluted" traffic. The causes were: (1) congestion on direct route; (2) rate cutting by weak, circuitous routes; (3) prorating practices in division of joint through rates; (4) desire for back-loading of empty cars; (5) interchange of traffic with connecting roads; (6) attempts to secure or hold shippers in contested markets. These remedies have been suggested: (1) more strategic location of plants; (2) the establishment of a base price plus the freight rate; (3) the restoration of pools and agreements. Centralization of administration has taught some good lessons in this regard also.

Intelligent, foresighted distribution and routing, speeding up freight through terminals, and more economical loading, can help but cannot cure an actual car shortage. On October 1, 1917, the railroads of the country reported that the excess of unfilled orders from shippers over and above idle cars at various points was equal to 70,380 cars. The idle freight car, like the Federal Reserve discount rate, however, is a sensitive barometer of trade. A great surplus of cars appeared as a result of the 1907 panic. An almost equally large shortage is shown in the figures for 1917. It appears that the entire railroad equipment is deficient. "The popular idea that the trouble is mainly due to car shortage is a narrow view of the question. Evidence indicates that traffic has outgrown the transportation plant; and that for more than a decade whenever business has been brisk, railway service has been inadequate and inefficient."[14]

**95. Demurrage.**—The freight car is not only a conveyance, but also a traveling warehouse. In this fact lies a danger, for the merchant may be inclined to be dilatory in unloading the material. To speed up the unloading the railroads make a demurrage charge after a reasonable period of time. When the broker, who has only desk-room in an office, tries to use the freight-cars as his warehouse, he meets with an accumulating charge that quickly eats into his profits. This charge began in 1887 when the evil of slow unloading was fully realized. The usual "free time" is forty-eight hours, after which a charge of about one dollar per day was made until this charge was raised by the Director General of Railroads. It is only fair for the railroads in their turn to be responsible for neglect in furnishing cars. The uneconomic methods of delaying cars, of reconsigning them, and of failure to collect demurrage charge have fast disappeared in recent years. The line between the function of the carrier and the function of the warehouseman must be clearly drawn.[15]

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[14] C. O. Ruggles, *Quarterly Journal of Economics*, November, 1918, p. 174.

**96. Trolley Lines.**—On the short haul much freight is carried in small lots by trolley. A study was recently made to show how a market may be controlled by the trolley lines serving it.[16] "The unsatisfactory and inadequate condition of the trolley freight service is due in the main to three reasons: (a) the difference in gauge or in wheel specifications, so that through freight cars cannot be run into the city; (b) want of proper traffic agreements; (c) want of interest in certain of the outlying trolley lines in the development of trolley freight."[17]

Such difficulties, however, are the mark of immature development, and are not inherent. There is no reason apparent as to why an efficient service in light traffic, such as milk, garden truck, small fruits, butter, eggs, and so forth, may not be secured. It is not difficult for a transportation system serving only a local community to adjust its schedules to local needs.

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[15] *Cf.* U. S. Department of Agriculture, Bulletin No. 191, "Demurrage Information for Farmers"; C. O. Ruggles, *op. cit.*, Nov., 1918, pp. 153-161.

[16] *Cf.* King, "A Study of Trolley Light Freight Service," *Annals of the American Academy of Political and Social Science*, Oct., 1912.

[17] *Ibid.*, p. 17.

**97. Motor-Truck Lines.**—With the continued improvements in highways and motor vehicles, motor-truck lines as a method of transportation will surely increase. This method is more flexible than that of steam railways or trolley lines. Motor-truck fleets were used during the war emergency to supplement the railways. Automobiles often deliver themselves for hundreds of miles. Regular trips are now made for considerable distances out from large market centers where the roads will bear the traffic. As has been stated, a single firm in Indiana has a fleet of twenty-five trucks. A truck has been used to carry cotton from the gin in Gainesville, Georgia, where the larger load and greater speed made possible the haulage of fifty times the amount carried by wagon. Forty bushels of potatoes were hauled to another market through one to two feet of snow. A maximum load of milk and garden truck was carried daily to Duluth from twenty-seven miles out. The goal of those interested in the development of this means of transportation is "to construct good roads everywhere and utilize motor vehicles entirely for local transportation, using railways and trolley lines for long distance haulage."

Movement of freight within a market center is, of course, dominated by the truck. In Chicago, however, there is a remarkable underground system of freight delivery. Trackage of 60 miles in length connects freight stations, and the principal warehouses and wholesale establishments. Nevertheless, the truck is the most effective means of city delivery to-day.

**98. Conclusion.**—The transportation system of the country is one of the most important commercial institutions.

In the marketing of many commodities it is strategic in getting control. The extensive pipeline system of the Standard Oil Company gave such an advantage in marketing that it was declared a public utility and was compelled by law to be accessible equally to all shippers. The highest degree of efficiency is necessary in performing the carrier function. Centralized control under government direction has achieved a mobility in freight-car service unknown before, and has cut down the car space needed for hauling commodities. For instance, coal shippers formerly sent 1,156 different kinds of coal to the Atlantic seaboard. Under centralized direction this was cut to 41. By a pooling of supplies arrangement, 133,000 freight cars were saved. Railroads have agreed to coöperate more thoroughly with water routes by exchange of traffic, by issuing joint bills of lading, and in connecting main lines to waterways.

The ideal of the carrier is to tap every resource and to serve adequately every market. This great task must be done effectively. For its fulfilment, there is required a stupendous organization, reaching out its tentacles into every hamlet and village, touching those little pockets of fertile valleys hidden away in the midst of vast mountain systems, serving all races, all climates, in all seasons. It is thus that "transportation becomes the basis of civilization," and is a "thing apart" from all other business organizations.[18]

## SUGGESTIONS FOR STUDY

It will repay the time spent in developing various points suggested in this discussion. Material is readily accessible, although for the most part not written from the marketing point of view. The following topics are suggested for this purpose:

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[18] C. S. Duncan, "The Uniform Bill of Lading," *Journal of Political Economy,* vol. xxv, p. 691.

1. The early beginnings of freight business in United States.
2. General features of early traffic.
3. The theoretical basis of rates.
4. Cost of service and value of service in setting rates.
5. Rate schedules.
6. The traffic departments.
7. Effect upon production and the market of the transportation factor.
8. Power of market control vested in the transportation function.
9. Importance of transportation cost in marketing.
10. The problem of routing freight.
11. The private car problem.
12. The refrigerator car.
13. Freight classification and tariffs.
14. Packing for shipment.

READINGS:

Haney, *Congressional History of Railways,* Chap. III.
Acworth, *Elements of Railway Economics,* Chaps. I, X.
McPherson, *Railroad Freight Rates in Relation to Industry and Commerce.*
Ripley, *Railroads; Rates and Regulation.*
Johnson and Huebner, *Railroad Traffic and Rates.*
Lasalle Extension University, "The Traffic Library."
Dunn, *American Transportation Question.*
Weld, *Private Freight Cars and American Railways.*
U. S. Department of Agriculture, Bulletin No. 191, "Demurrage Information for Farmers."
U. S. Department of Agriculture, Report No. 98.
U. S. Department of Agriculture, Bulletin No. 74.
Thompson, *Cotton Field to Cotton Mill,* Chap. XIV.
King, "A Study of Trolley Light Freight Service," *Annals of the American Academy of Political and Social Science,* vol. 1.
Tissenden, *Industrial Traffic Management.*
*System,* Nov. 1916, pp. 517-26; Aug. 1917, p. 202; July, 1916, pp. 102-9; Aug. 1916, pp. 145-7; Sept. 1917, pp. 319-21; July 1917, pp. 54-56.

U. S. Department of Agriculture, Farmers' Bulletin 703.

Chicago Chamber of Commerce, "Chicago: Its Transportation Facilities."

U. S. Department of Commerce, "The Transportation of Petroleum."

U. S. Department of Agriculture, No. 701, 1916, "Possibilities of Market Train Service."

For further bibliography see bibliography published by the Bureau of Railway Economics. Each student should now prepare a discussion of the transportation problem as it affects the commodity which he has investigated.

# CHAPTER VII

## ORGANIZED EXCHANGES

**99. What an Organized Exchange Is.**—An organized exchange, as the term is used here, includes all types of produce exchanges as well as those dealing in cotton, coffee, iron and steel, tobacco, etc. It may be defined as an organized market "which enables people to buy and sell, freely, certain commodities either in person or through a broker; and which in order to facilitate such trade has for its fundamental object the promotion of uniformity in customs and usages, the inculcation of principles of justice and equity in trade, the facilitation of the speedy adjustment of business disputes, the dissemination of valuable commercial and economic information, and the securing to all its members all the benefits of coöperation."[1] "This chamber of commerce" [Chicago Board of Trade], said the Supreme Court of the United States, 1905, "is, in the first place a market where, through its 1,800 members, is transacted a large part of the grain and provision business of the world. Of course, in a modern market contracts are not confined to sales for immediate delivery."[2]

It is clear that the phrase "organized exchange" has acquired a semi-technical meaning. In one sense, a department store, a bank, a warehouse, or even a trade center itself may be called an organized exchange, that is, an organization which in some way controls and directs the interchange of goods. The distinguishing feature must be the purpose of organization, which should be to furnish an open market under standardized practices for one or a group of commodities. In Chicago, for example, there are three of the greatest organized exchanges in the world, namely, the Chicago Board of Trade, the South Water Street Produce Market, and the Union Stock Yards. Besides these, there are minor markets, like the Butter and Egg Board, the fruit auction, and the subsidiary produce markets. The Stock Exchange for the purchase and sale of stocks and bonds is purposely omitted.

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[1] Huebner, *Annals of the American Academy of Political and Social Science,* vol. xxxviii, p. 3.

[2] 88 Fed. 868.

Each of these exchanges combines several functions for the handling of certain products. It is wise, however, to distinguish clearly the difference between these institutions and the functions performed in connection with them. Commercial grading of a commodity may be essential to the dealing in future contracts, but grading is not a unique function of an organized exchange. Market news may be necessary for intelligent activity on an exchange, but market news is quite necessary for intelligent action in any line of business. Buying and selling for future delivery may take place without connection with anything that could be called an exchange. The fundamental, distinguishing feature of an organized exchange is that it is a continuous, open market, organized under agreed practices and conditions. Many important consequences flow from these characteristics.

**100. Functions of Organized Exchanges.**—In the popular mind the chief function associated with stock, produce, or other exchanges is speculation, that is, buying and selling for future delivery. A moment's reflection, however, will reveal the fact that buying and selling for future delivery is a very common characteristic of business. But, of course, the meaning is the buying and selling of contracts to deliver in the future, in many cases without any intention of asking for actual delivery of the commodities or of being able to deliver them. This type of speculation is characteristic of organized exchanges, although probably a result rather than a cause. The primary function of an organized exchange is to bring buyer and seller together. For this purpose there must be an open, continuous market or well-known regulations, so that buyers will not be disappointed when they come to meet sellers, and *vice versa.* If the producer of livestock starts for Chicago or Kansas City or St. Paul with a carload of cattle, from a point hundreds of miles away, he must be assured in advance of a place where he can offer his cattle for sale to buyers who will come to that place to buy. This open market feature is basic, is fundamental to an organized exchange. Practically all other functions flow from it.

The organized exchange, to be successful, must make it easy and economical for buyers and sellers to meet and to transact business. Once more, it is a question of the best way of doing things. Thousands of keen business minds are seeking eagerly for better, more economical methods. The organized exchange, like every other business institution, must stand this acid test of competition. There will be found, therefore, in every successful exchange the means provided for each buyer and each seller, himself, or through an agent or a broker, to transact business with ease and with economy.

Not only must dealings through an exchange be easy and economical to make, but also they must be done with speed. Time is of the essence here. It is not a matter of weeks, months, or years, but of minutes and seconds. A deal in wheat was put through some time ago between a broker in Liverpool and another in Chicago, in which the Liverpool broker asked for quotations and the possibility to deliver the amount of wheat desired, received the answer, and sent back the acceptance, all between ten and twelve o'clock, on a single morning. The most efficient paraphernalia possible is required to expedite every transaction.

Part of the equipment which an organized exchange must have to perform the previously mentioned functions is the best available telephone and telegraph service; the mechanism for securing contact with buyers and sellers; for grading, weighing, inspecting; and a means of keeping in constant touch with every development in the field of production and consumption. The organized exchange becomes, therefore, in itself a secondary mechanism through which the risks of distribution are concentrated and are dealt with in the most nearly scientific manner possible. "Why has the commercial distribution in the United States become so largely identified with the speculative class of trading capitalists? The answer is that it has been found best for the producing and consuming interests of the community that the risks of distribution should be localized in a separate commercial class whose members are in a position to inform themselves as to all the factors—past, present, and prospective—affecting the future course of prices."[3]

The organized exchange becomes, therefore, a sublimated brokerage firm. In it contracts are bought and sold by brokers. But it becomes, as an open, continuous market, of more influence than any private brokerage firm can become. "Upon that market is concentrated, in a sense, the judgment of every human being in the world having any interest in production either as consumer or producer."[4] Whatever may be the abuses perpetrated through organized exchanges, when they function properly, they afford the best known medium for the intelligent working of supply and demand. "They focus intelligence from all lands and the prospects for the whole year by bringing together minds trained to weigh such intelligence and to forecast the prospects. They tend to steady the markets more nearly to their right level than if left to chance or unhindered manipulation.''[5]

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[3] Fayant, *Some Thoughts on Speculation*, p. 23.

[4] Conant, *Function of the Stock and Produce Exchange*, p. 30.

As services to be rendered by a properly functioning organized exchange may be mentioned: (1) exchanges give mobility to capital and to commodities; (2) exchanges become great clearing houses of trade information; (3) exchanges steady market prices by making possible the discounting of the probable effect of an anticipated or known event; (4) exchanges help to regulate the rate at which the year's crops are consumed; (5) exchanges serve to level prices in different markets; (6) exchanges afford a test of utility of any commodity to the community by giving expression through price changes to the community judgment; (7) exchanges, by means of speculation, are probably among the chief directive forces in trade and industry; (8) "The markets furnished by organized speculation represent the most complete development of the competitive system and of democracy in trade, as opposed to monopoly and concentration of wealth and power;''[6] (9) exchanges distribute the risks among a special commercial class, that is particularly equipped to bear them; (10) exchanges afford an effective mechanism through which grading of commodities, market information, and other market functions may be performed.

**101. Produce Exchanges.**—The term ''produce'' is generally understood to mean perishable provisions such as vegetables, fruit, butter, eggs, fish, poultry. A produce exchange, or organized produce market, then, is one which handles such commodities. An exchange of this kind will be found in all trade centers of substantial proportions. One of the largest of these markets to be found anywhere in the world is the South Water Street Market in Chicago. This great market has developed to meet the increasing demands, but in general its organization has not kept pace with its growth. The most influential single organization is the Wholesale Grocers Exchange, but there is not here the perfected mechanism that may be found in the stock or grain exchanges. While a daily rate sheet, the official bulletin, does circulate, there is not the possibility of ascertaining the "visible supply," *i.e.*, the amount on the way, or the prospective supply. The live poultry dealers, alone, have central meetings daily at 9:30 A. M. Receipts and varieties are posted and the dressers come there to bid for stock. Here is emerging the same type of organization that has developed elsewhere.

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[5] Judge Grosscup, 88 Fed. 868.

[6] Brace, *The Value of Organized Exchanges,* p. 225.

Although lacking in the perfected organization of other types of markets, the produce market performs with reasonable effectiveness the functions necessary. It affords an open market. The shipper of produce, wherever he may be, knows that there will be a possible sale at some price for his produce, knows that dealers capable of handling his produce will be there to take charge of it. It is equipped to handle any amount of produce without notice; it attracts buyers; it makes possible the meeting of buyers and sellers; it affords a speedy means of getting perishable produce to retailers and consumers. The necessary paraphernalia is also provided.

The dominant middleman in the South Water Street Produce Market is the jobber. Commission merchants and brokers are there, too, but according to a report made by the Municipal Markets Commission suspicion on the part of producers of all middlemen who would not buy outright has somewhat discredited them. To this market come two general types of buyers, the retailers and the peddlers. The carts of these two buyers are sent to the market early in the morning, usually from 5 A. M. until 9 A. M. Large retailers send their own wagons; small retailers expect to have their purchases delivered or to be served by peddlers.

Produce reaches the market by rail or water, usually, although the farmers and truck gardeners haul in their product direct in some cases. What is shipped is usually consigned to some dealer who is not always forewarned of its dispatch. Lack of competent organization may be found everywhere, and much complaint with the marketing methods may be traced to this fact.

The South Water Street Produce Market may be taken as a type. Similar ones may be found in New York, Boston, Philadelphia, Baltimore, Washington, and elsewhere. The demand to perform the same functions has produced the same kinds of institutions. Municipal markets for handling produce are so like this example in all essential features that they need not be described. The real issue between produce markets under private management and those under municipal management is not one of function or organization but of control. Should the control be left in the hands of individuals or should it be assumed by the municipality?

**102. Grain Exchanges.**—The grain exchanges are, next to the stock markets, the most highly developed market organizations. At bottom these exchanges are founded on wheat, although they handle other things, such as corn, oats, rye, flaxseed, cotton-seed, hay, as well as provisions, that is, cured meats. It has been said that the most nearly perfect marketing machinery in existence has been developed to handle wheat. It has a world-wide market and it is grown over a widely-extended productive region; it is not readily perishable and it has a flowing quality that aids in handling it; the value relative to weight and bulk is such as to carry it to any market. Of greater importance to the organized exchange, it can be graded according to general standards.

In distinction from the produce market, the grain exchange is dominated by the broker. This fact is significant. It means that the exchange deals largely with contracts for grain, rather than with the grain itself. There are two fairly separate parts to every grain exchange. One is called the "spot" market and the other the "futures" market. In the "spot" market, grain is bought and sold by sample in carload lots. Here the middleman is usually a commission merchant or jobber. The grain is actually in existence, on board a car or in an elevator. If this part of the organization stood alone, it would not differ from the conduct of business by many other commission merchants and jobbers. It is, however, not wholly separated from the "futures" market.

The substance of the "futures" market is the contract. In September one may buy or sell December or May wheat, which means the delivery of the amount contracted for, sometime during the month named, the actual time to be set by the seller. So at the other periods, July and September grain may be bought and sold. These contracts may change hands often and may be, and many often are, cancelled without demand for actual delivery. It is for the conduct of business in these futures that all of the paraphernalia of the grain exchange is required. This is speculation.

Such speculation is carried on by brokers, who are members of the exchange, according to the rules and regulations adopted by it. These brokers are not permitted on the Chicago Board of Trade to buy and sell on their own account. In all of their transactions they are agents of their clients. Whatever "inside" information they may get, whatever "tips" on the market, are presumed only to make them more expert, more fully equipped to act intelligently as agents. Their returns are based upon the amount of sales made, a standardized commission being charged.

Membership is transferable. Dealing on the grain exchange must be by members only. But these brokers are eager to do business because the greater the business the larger their returns. They maintain, therefore, an open market.

Sales on the grain exchange may be made, therefore, in two distinct ways, by sample in the "spot" market, and by contract on grade in the "futures" market. The former is the work of a grain commission merchant; the latter of a grain broker. Through either of these channels grain may be sold at any time and in any amount above a stipulated minimum, which for wheat is 5,000 bushels. Quotations are published in the papers and are spread broadcast throughout the country on the "ticker." It is an open, public market in every sense.

One particular method of sale is especially characteristic of the grain exchange, and indeed of other exchanges where "futures" are dealt in. It is "hedging." The dealer who does not wish to bear the risk of fluctuating market prices, the flour dealer for instance, may transfer that risk to the exchange by a double transaction. He may desire 50,000 bushels of wheat per month to grind. To get it, he will buy for future delivery that amount, at the price quoted on the exchange. At the same time he may sell for future delivery an equal amount of wheat. Then if the market price falls or rises, what he may gain in the one deal he will lose in the other. Market fluctuations, however great, cannot affect him. Freed from the risks attending unforeseen changes in market price, he can devote himself solely to a manufacturer's profit. This method of dealing characterizes all exchanges where future contracts are bought and sold; it is placing on the shoulders of a professional class of speculators the special burden which they should carry. It is a kind of business insurance.

**103. The Cotton Exchange.**—Cotton exchanges exhibit the same essential characteristics as the grain exchanges.

There is, to be sure, a different technique because of the different qualities of the commodity, but otherwise the exchanges are fundamentally the same. There are to be found here, also, brokers and commission men; "spot" sales and "future" sales; hedging; all the paraphernalia for handling the commodity and for grading it; all the machinery for collecting market news. The great bulk of cotton transactions is made as easily, speedily, and economically as possible.

In the cotton exchange there are nine classes of dealers. There are the commission merchants who sell cotton for the planters; there are exporters who buy cotton for the foreign market; there are merchants who buy cotton for the spinners in the United States; there are the bankers through whom all bills of exchange drawn against cotton are negotiated; there are ship agents who represent the great fleet of steamers and sailing vessels by which cotton is carried abroad and to domestic ports; there are the insurance agents who arrange the insurance on the bulk of the cotton seeking a market through each port; there are the cotton brokers; there are the expert judges of the raw material, who buy cotton from representatives of the planters for the merchants who ship to Europe and to American spinners; there are the "future" brokers who buy and sell contracts for delivery in the future for the account of members of the exchange or for merchants and spinners in Europe and the United States.

The methods of doing business on the great cotton exchanges, and especially on the New York Exchange, have in the past been deleterious to the trade. Future contracts were deliverable on basic grade; that is, so many units, "50,000 pounds or about 100 square bales," were bought for future delivery, without specification as to grade. Any standard grade within set limits could then be delivered on the contract by the payment of a fixed difference in price per grade above or below "middling," which is the "basic" grade. As a result, the spinner could never be sure that he would have delivered on his contract a grade of cotton that he could use. It came to be the prevailing custom to deliver grades lower than "middling." The price differences between grades, also, were unfair to buyers.

As a consequence there was passed on August 11, 1916, the Cotton Futures Act, definitely limiting the deliverable grades, and establishing grade standards by scientific tests made by the Department of Agriculture. It is also definitely stipulated by law that there shall be only two cotton exchanges where future contracts can be bought and sold. These are the New York and New Orleans exchanges. In like manner, there are fifteen "spot" markets designated; Atlanta, Augusta, Boston, Charleston, Dallas, Fort Worth, Galveston, Houston, Little Rock, Memphis, Mobile, Montgomery, New Orleans, Norfolk, and Savannah. Eleven out of this list have been selected as places where the differences above or below the contract price to be paid for grades tendered or delivered on the contract are determined from actual transactions.

The sole purpose of this act is to regulate conditions within the cotton exchanges so that they will function properly. The situation in the cotton exchange of New York was such that the New England spinners who bought on grade, that is, for future delivery, could not be assured that the cotton actually delivered to them would be of such sort that they could use it at all. It became a common experience that the great bulk of cotton really delivered on exchange contracts was below, and a large proportion far below, the basic grade. Furthermore, the fixed differential in price gave the advantage to the seller. As a consequence, the amount of cotton dealt in on the New York Exchange fell off. So necessary, however, was the existence of a central organized market, that it was felt to be far better to correct the error than to dissolve the organization. This is proof positive of the value of the service rendered by the institution. Under the Cotton Futures Act the grade differences are now based upon the "average actual commercial differences in value" prevailing in not less than five of the *bona fide* "spot" markets listed above.

104. The **Coffee Exchange.**—Coffee, also, is bought and sold on grade and there is an organized exchange in New York City to handle it. This commodity differs from grain and cotton in that it is an import, while the others are largely exports or for home consumption. A very large part of the coffee brought into the United States comes from Brazil, and must pass sooner or later into the hands of roasting concerns. Ninety-seven per cent of the coffee imported passes through the New York exchange.

There are two kinds of markets for coffee, as for grain and cotton. One is the "spot" market and the other is the "exchange" market. In the latter market, which operates under rules and regulations, coffee is traded in on the basis of future contracts. The basic grade is called No. 7, which is established by the rules of the trade. The exchange also "licenses the necessary coffee graders, warehousemen, weighmasters, and samplers of the exchange."[7]

In the coffee exchange there operate the same groups of middlemen as in other exchanges. Brokers, commission houses, roasters, importers, warehousemen, all appear. Sometimes the broker will suddenly turn jobber by purchasing a cargo while on the way, thus gaining full title to it and assuming all the risks for it. Unless he can sell the cargo before it arrives, he must arrange for its unloading and warehousing. These middlemen have developed the same type of organization, as is true of grain and cotton and produce, to secure market information and to enable the free play of world forces, so as to establish a world price.

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[7] *Annals of the American Academy of Political and Social Science,* vol. xxxviii, p. 297.

**105. Butter and Egg Board.**—A special organized market has been developed in various sections of the country to handle butter and eggs. In Chicago, there is a Butter and Egg Board, duly incorporated to handle butter and eggs; it has its constitution, its by-laws and its "butter and egg rules"; it appoints its own butter and egg inspectors (By-laws, Sec. 7); it regulates the methods of sale; it establishes grades; it designates methods of sampling; it arbitrates disputes; it makes possible the dealing in spot sales and in future contracts. "Spot sales shall be paid for when delivered unless otherwise agreed" (Sec. 4). "The time on all sales of butter on the 'call' for future delivery is limited to ten days" (Sec. 12).

Much criticism has been leveled against the methods of the organized exchanges which deal with dairy products. They have been accused of manipulation, of not being open markets. Gradually, however, the business is being toned up. Every business institution in its development passes through its stage of unethical methods. While bad business practices are never to be condoned, at the same time the institution itself should not be condemned because of its misuse by unscrupulous dealers. Wherever the organized exchange can operate freely it has proved its worth. Its own members have been educated by experience to higher ethical standards. In so far, then, as dairy products can run on grade, in so far as there can be installed a truly open market, in so far as the dealers on the board are carefully disciplined for misconduct, the organized exchange will justify itself as an economical marketing method.

**106. Stockyards.**—There have developed in several trade centers of the Middle West organized markets for livestock. Among these are stockyards in Chicago, St. Louis, St. Paul, Kansas City, Fort Worth, and Denver. They may well be called livestock exchanges. Because livestock cannot be bought and sold on grade, since it must be inspected and judged by experts, there is no futures market. All sales in the stockyards are spot sales. The cattle and hogs and sheep and horses must be in the stockpens when the trading is done. In this fact lie both an advantage and a disadvantage for the seller. In the first place, there must be the equipment for taking care of all livestock that comes in. This means a continuous, open market; on the other hand, the livestock shipper cannot long withhold from selling, because his is a perishable commodity.

In the trade centers named above, and in others, there are organizations to regulate and to standardize market practices in handling livestock. A flat charge is made for the use of stockpens; a standard charge is made for feed; all stock arriving must be cared for; a standard charge is made by all commission men, who are the predominant type of middlemen in the stockyards; to these stockyards come the buyers. Here are all the characteristics of an organized spot-sales market.

The main types of dealers in the stock-yards are: (1) the commission men, (2) the stock jobbers, (3) the buyers for the small packers, (4) the buyers for the big packers, (5) the cattle feeders, (6) the Eastern buyers, (7) the foreign buyers. The commission men have charge of certain stockpens and receive the livestock on consignment or take charge of it when the shipper arrives, grade it so far as practicable, and sell on commission. The stock jobber may buy a drove of cattle, hogs, or sheep to speculate with, believing that the price will rise before the day's market closes or feeling that by grading he can split the sales between feeders and packers to his own advantage. The different classes of buyers are described by the terms used. Alongside the stockyards are the packing plants of the big packers. They are undoubtedly the most potent factor in the market. Their buyers are waited for eagerly, and their bids are a tremendous factor in establishing the day's market price. They are shrewd, careful buyers and know full well how to drive a close bargain; they are deeply learned in the psychology of higgling in the market. The small packers usually try to pick up the stock they need early in the day, take odd lots, or wait until late for remnants. The foreign and Eastern buyers are becoming a smaller and smaller factor as the tendency grows to ship meat instead of livestock.

The stockyards, like the produce exchanges, will be able to function satisfactorily only when the buyers and sellers meet on a more nearly equal footing. As it is, the sellers have brought in a perishable product from their homes, often hundreds of miles away, and must sell or sustain an increasing loss within the space of a few hours. The market opens at seven o'clock in the morning and the sales are practically over by one o'clock. The buyers of the big packers, on the contrary, are fully acquainted with the relative amount of livestock to arrive each day; they know how many of each grade they need to make up their weekly "pack"; they are thoroughly versed in the psychology of discouragement; they have learned by experience how to gauge the encouragement to be given to shippers for bringing in the necessary livestock; they have up-to-the-minute information on the wholesale meat market.

The livestock shippers have been guilty of poor business practices. They have sent unhealthy animals to market; they have given them heavy feedings just before arriving at the yards. If the two parties are to try to get the advantage of each other without regard to good business ethics, there will always be much complaint. The conditions of the past have inclined the public to demand that the stockyards be declared public utilities and thus come under the supervision of public utility commissions. The packers have often been accused of owning and manipulating these organized markets for their own advantage. To function properly, they must, like the grain exchanges, be truly open markets, doing business under strict principles set forth by the organization itself.

**107. Wool Market.**—There is no organized market for future trading in wool. Like produce and livestock, it cannot be sold on grade, but must be inspected, sampled, and judged. A well-trained expert is required for buying wool intelligently. While in the grease, it must be judged as to amount and quality when scoured. In the wool trade a judgment is called bad that misses the result by more than 1 per cent.

There is no great, organized wool market in the United States to compare with those of London and Antwerp. These great, organized markets are spot-sales markets and are called auctions, because the wool is actually auctioned off. An attempt was made in 1894 to establish the New York Wool Exchange, but it proved to be a failure. It is interesting to note that several of the functions of an organized exchange in wool are performed by the wool merchant in such Eastern markets as Boston, New York, and Philadelphia. These functions are performed in connection with the warehousing of wool. It is the duty of the wool merchant to offer to spinners an open, continuous wool market, where they can come at any time and secure the amount and the quality of wool they desire. Grading, market information, financing, concentration of supply are all within the duties of the wool merchant. The large concentration warehouses in the East afford the nearest approach to an organized exchange. The strategic position of the wool merchant has already been indicated.

If the wool-marketing methods of the United States are capable of material betterment, it is along the line of increasing the efficiency of the wool merchant's methods and equipment, and not by the elimination of this type of middleman. . . .

If the economic pressure should put a stop to the careless methods of growing and packing wools which have characterized the American industry for so long, and if the possibilities of substantial profits from wool growing under better methods should be demonstrated beyond dispute, then it would not be long until domestic wools would appear in the market on an entirely new basis. Much of the present speculative element of the wool merchant's functions would be gone. Auction sales, both at local points in the West and at the chief Eastern buying centers, would become both possible and desirable.

Whether this would mean the "elimination of the middlemen" and more direct contact between growers and mills is by no means certain. But it is certain that much of the speculative lure would be removed from the wool merchant's business as it is at present conducted. As an assembling business done on a narrow margin and depending on volume of profits, wool-dealing might not be as attractive a business as it now is. It might still perform an indispensable function and do it more effectively and at less cost than it could be performed by direct sale. Better wool growing, better wool, and better preparation for the market may mean radical change in the work of the wool merchant, but they do not necessarily involve his extermination.[8]

**108. Iron and Steel Institute.**—A relatively loose organization has developed in the iron and steel industry. It may be said that there is no distinct, organized exchange to handle these materials. In New York there is an exchange which deals in "iron warrants," but it has never attained much influence. However, most of the functions of the organized exchange are performed either by the great steel companies themselves or by the American Iron and Steel Association and the American Metal Market Co.

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[8] Cherington, *The Wool Industry,* p. 73.

As will be shown later under market information, the essential function of these associations is the collection and dissemination of the current news of the iron and steel industry. There are, in particular, the *Daily Iron and Steel Reports* and the *Steel and Metal Digest.*

It must be remembered that the production of ore can be substantially controlled because of centralized organization; it is also to be remembered that iron and steel are very largely manufactured on order, and that between 80 and 90 per cent of the entire output of pig iron is used by the plants making it, for further fabrication. This leaves a very small percentage for open market purposes. Obviously, the character of the productive organizations and the character of the commodity do not demand the services of a great organized exchange. On the financial side, however, through stocks and bonds, the functions of the highly developed stock exchanges are utilized.

**109. Sugar Exchanges.**—At present there are but two sugar exchanges in the United States; one in New York, and the other in New Orleans. The New York exchange handles only raw sugar. It also, unlike the New Orleans exchange, deals in "futures," a comparatively new feature in the sugar industry of this country. These future transactions have a tendency to minimize seasonal depressions due to the natural scarcity of stock during certain months, and tend to promote a uniform price. The New Orleans Sugar Exchange deals in "spot transactions" and is the only commercial body in the world which devotes itself exclusively to sugar. It is ideally located for warehousing and shipping. Here information is received from all parts of the world as to the size of and prospects for the world crop. The American Sugar Exchange and the Sugar Equalization Board took over largely the functions of the organized exchanges during the war.

The advantages of the sugar exchange are: (1) It provides an open and continuous market, and brings the buyers and sellers together, the refineries buying their sugar on the New York Exchange; (2) it gives the quality of mobility to the sugar crop; (3) it steadies price; (4) it helps to regulate the rate at which the year's crop is consumed; (5) it tends to level out the market price. As has been shown, these are the *bona fide* functions of an organized exchange.

**110. The Auction.**—As an institution the auction is not new. The primary principle is that of an open market where all buyers may come and where the goods for sale are "knocked down" to the highest responsible bidders. An auction may be held with or without an organization. The professional auctioneer is familiar to many sections of the country. When a farmer desires to move to a new part of the country or to quit farming, he may want to sell off his livestock, vehicles, crops, and household goods. A date is then set for a public auction. Or property may be sold at auction for taxes; auctions may be held to dispose of blooded livestock. In the cities auctions are often held in jewelry stores. The street fakir sells patent medicine at auction. Tobacco may be sold in the warehouses at auction. Furs are sold at such auctions. The most highly-developed permanent organization for an auction market is to be found in the fruit trade.

It is the type of auction that handles citrus fruits and other highly-perishable fruits that approaches most nearly to the organized exchange as defined here. To secure such an organization there must be a continuous supply of commodities, such as will justify an open and continuous market. This is a simple, direct, although somewhat crude, method of marketing. Quick action does result, for the entire lot, often comprising many carloads of produce, can be sold within a few minutes.

Beginning at five o'clock in the morning, through the summer months, the buyers appear in the large warehouse room where the produce is on display. Samples of each lot are open for inspection, and the buyers move from one

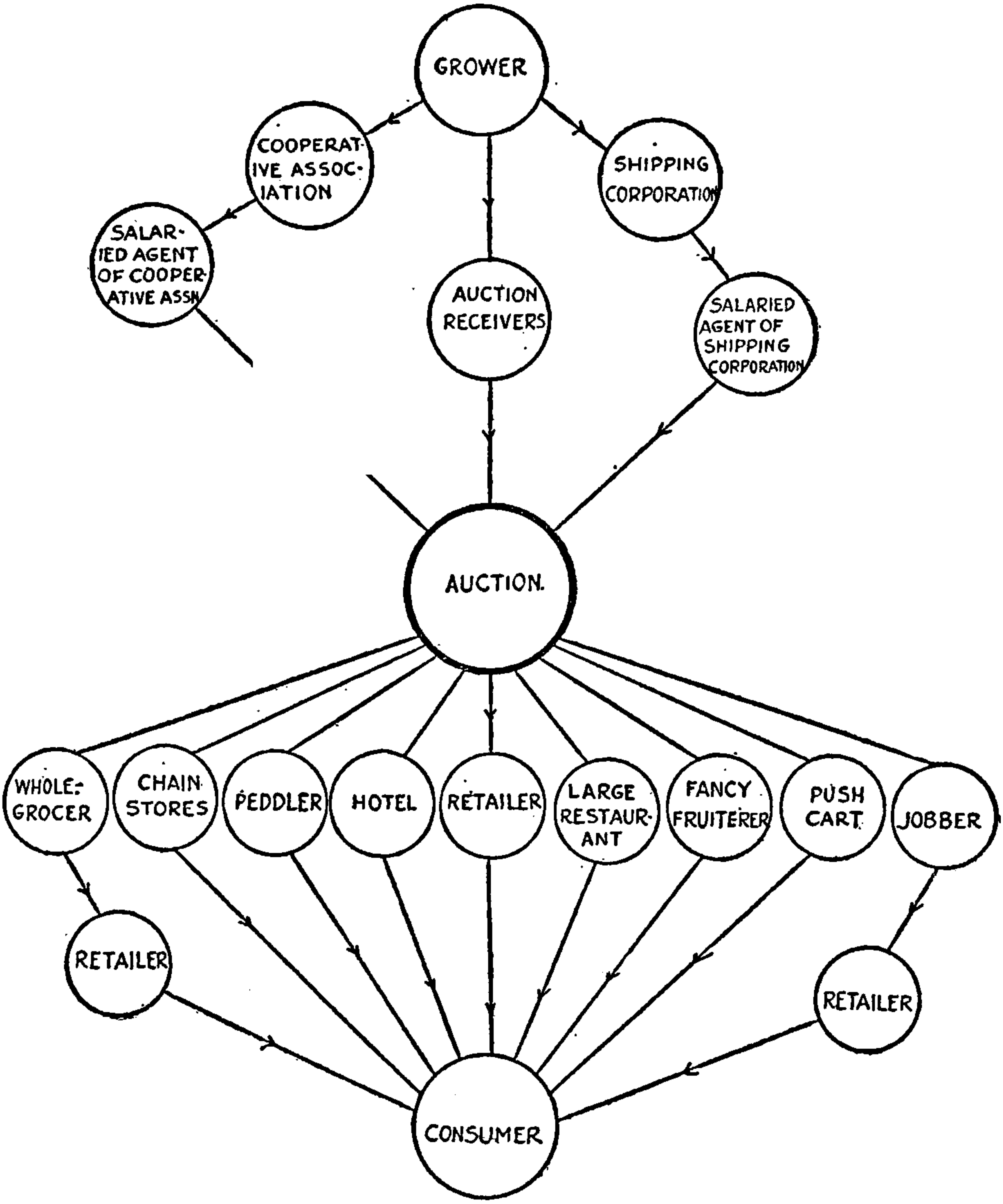
GROWER
COOPERATIVE ASSOCIATION
SALARIED AGENT OF COOPERATIVE ASSN
AUCTION RECEIVERS
SHIPPING CORPORATION
SALARIED AGENT OF SHIPPING CORPORATION
AUCTION.
WHOLE: GROCER
CHAIN STORES
PEDDLER
HOTEL
RETAILER
LARGE RESTAURANT
FANCY FRUITERER
PUSH CART
JOBBER
RETAILER
RETAILER
CONSUMER

CHART OF THE AUCTION SYSTEM OF HANDLING PRODUCE
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consignment to another jotting down notes against each one on the advance sheets of receipts that are handed around. At seven-thirty or later a bell rings and the buyers go up to the "school-room," *i.e.*, the auction room filled up with school-room desks. The buyers seat themselves; the auctioneer takes charge; the tally sheets are corrected, *i.e.*, broken boxes, number of boxes, etc., are indicated. The auction then continues after the typical manner of auctions.

These auctions, which exist in fifteen or more cities, work under established rules, handle produce on grade, supply information as to the amount and quality of arrivals, and maintain a continuous, open market where buyers and sellers may meet, as do all organized exchanges. It is a unique characteristic of the auction that the selling is concentrated in the hands of one man, the auctioneer. In the grain exchange all brokers are auctioneers. A graphic picture by the advocates of the auction method of handling produce is given in the chart reproduced on page 153.

**111. Cooperative Organization.**—An organized exchange may take the form of coöperation. The most conspicuous example is that of the California Fruit Growers Exchange. The headquarters of this gigantic organization is in Los Angeles, from which, by means of the telegraph, sales are made in all of the important trade centers.

The California Fruit Growers Exchange is composed of one central exchange, 17 district exchanges, and a large number of local producers' associations. The central exchange on the one hand represents the producers and on the other directs the business of selling. Through it the growers and sellers communicate. The sellers receive their orders from the growers and are thus controlled by them. If one will think of a telephone exchange into which lead a great many wires and out of which lead a great many more, one will be able to see much more clearly the services of the central exchange.[9]

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[9] C. S. Duncan, "Concentration in the Marketing of Citrus Fruits," Community Leaflet No. 20, p. 18.

This organization, and others built on the same type, perform the same functions as other organized exchanges. The fundamental difference is that it represents only one side of the market, namely, selling. The purpose is to retain for the growers all their independence of will and action and at the same time gain for them all the advantages and economies of large-scale distribution. By means of centralization in a coöperative exchange, the growers can meet the buyers in the market on equal terms, without losing a whit of their individuality and independence. Men coöperate either to buy or sell. A coöperative organization, therefore, like the auction, is intended only for one half of a true open market. Sellers and buyers are brought together, to be sure, but the organization itself is brought into being to aid one side; it is not a real exchange.

**112. Municipal Markets.**—There is no new principle in municipal markets. Their organization must be able to perform the same functions as that of any other kind of exchange. The difference is in control. In the one case it is in the hands of a private organization, in the other it is vested in the city. The sole question at issue is whether the services will be performed more efficiently in the one case than in the other. This issue does not fall within the scope of this discussion.

**113. Speculation as a Commercial Problem.**—H. C. Emery says of speculation on stock and produce exchanges in the United States:

> Speculation has become an increasingly important factor in the economic world without receiving a corresponding place in economic science. In the field in which it acts, in the trade in grain and cotton and securities and the like, speculation is the predominant influence in determining price, and as such it is one of the chief directive forces in trade and industry. . . . The stock and produce exchanges are the nerve centers of the industrial

body, and are in themselves as necessary institutions as the factory and the bank.[10]

The main point to consider in this connection is the fact that a real *bona fide* transaction, a real buying and a real selling, takes place, and that the buyer and seller satisfy all of the legal and other obligations, and possess the same rights and responsibilities, and title to the goods, that attend any other kind of transaction. "Speculation of this kind by competent men is the self-adjustment of society to the probable. Its value is well-known as a means of avoiding or mitigating catastrophes, equalizing prices, and providing for periods of want."[11]

Speculation is the attempt to determine not only what is, but also what is to be, the demand and supply of any given commodity. Therefore, such exchanges as those described above have built up great organizations for securing trade news and for transmitting it quickly. Every event, actual or probable, anywhere in the world, affecting the marketing of a given commodity finds quick reflection on the exchange, and with equal speed, by means of buying or selling, and thus affecting prices, adjustment is made in accordance with the event. This process is called discounting the future, and has been presumed to stabilize the market, to steady the price.

Great fluctuations in price come usually from catastrophe or ignorance. Knowledge is the great price stabilizer.

Where there is a high degree of certainty, prices will be as stable as conditions permit, and more can not legitimately be expected. Insistence upon the advisability of emphasizing the degree of certainty does not in any way imply that the reasoning about speculation and prices is wrong. The doctrine that speculation tends to stabilize prices is true, but it states only part of the truth. With reference to the recent improvements in marketing, increase in relative stability of prices has been significant. The conspicuous change lies in the great increase in certainty.[12]

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[10] Emery, *Speculation in the United States,* p. 290.

[11] 88 Federal 868.

The peculiar type of speculation, the dealing in future contracts without the expectation to give or require delivery, has led to the development of a marvelously sensitive mechanism for the adjustment of price. The most vital part of this mechanism is market news. Without market news an organized exchange would have no advantage; with it, there results the "struggle of well-equipped intelligence against the rough power of chance."[13]

**114. Conclusion.**—A review has been made of the organized exchange, its definition, its functions, and its various types. Something has also been said of the value of speculation so commonly associated with the organized exchange in the popular mind. No attempt has been made to appraise the exchange, or to defend or criticize its activities. It is obvious to any observer of business methods that many of them are correcting themselves. Of their importance to-day there can be no question. If they do not correct themselves, the public will demand that they become public utilities and pass under regulation.

### SUGGESTIONS FOR STUDY

The student should study the organized exchange in relation to the commodity that he is investigating. For classroom work the following topics may be taken up for discussion:

1. When and why an exchange is needed.
2. Organized exchanges as a means of market control.

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[12] Usher, *American Economic Review,* March, 1916, p. 60.

[13] Emery, *op. cit.,* p. 463.

3. The producer's interest in exchanges.
4. Interest of dealers in exchanges.
5. Consumer's interest in exchanges.
6. Character of commodity, of market, in relation to organized exchange.
7. The clearing house of the exchange.
8. "Ringing out" on the exchange.
9. Control of exchanges.
10. Place of the organized exchange in commercial organization.

READINGS:

Brace, *Value of Organized Speculation.*
Emery, *Speculation in the United States.*
Huebner, *Agricultural Commerce,* Chap. IX.
Weld, *Marketing, Farm Products,* Chap. XV.
*Annals of the American Academy of Political and Social Science,* vol. xxxviii.
U. S. Department of Commerce, "Report of Commissioner of Corporations on Cotton Exchanges."
McHugh, "Form, Development, and Economic Function of the Grain Exchange," *Annals of the American Academy of Political and Social Science,* vol. xxxiii, pp. 1-35.
Fayant, *Thoughts Upon Speculation,* Chap I.

# CHAPTER VIII

## THE WAREHOUSE

The warehouse is an ancient and honorable institution, having long been known through the story of Joseph and his storage of corn in Egypt during the seven lean years. Its real beginning, however, fades away into unrecorded antiquity. But the history of the warehouse is not a part of this discussion. Within recent years there has been such a remarkable development of warehousing, particularly for the great staple crops, like cotton and grain, and in cold storage, as to make the industry a practically new one. In the discussion, narrowed in this way, the attention will be concentrated upon function rather than upon descriptive detail.

**115. Recent Developments in Warehousing.**—In the "Warehousing Industry in the United States," published by the U. S. Department of Commerce and Labor, the progress of warehousing is commented on as follows:

> The problem of caring for the commercial surplus of the annual output of industry and of keeping in custody that reserve of storable utilities not required at any given time by the community has, within the last decade, become an increasingly important feature of business in the United States. This division of enterprise is usually spoken of as the warehousing industry, including storage, transfer, and cognate activities. The progress of cold storage has given a technical turn to warehousing which was entirely foreign to it twenty-five years ago, but which has done more than anything

> else to put the warehousing industry on a scientific basis. It is not too much to say that every other branch of storage has been favorably affected by the systematic methods of refrigeration. The development of this mode of preserving perishables is, however, probably due as much to the transporter as to the warehouseman. Commerce seems first to have seen the necessity of discovering some method of preserving food supplies in the course of transportation between the most favorable areas of production and the best markets for consumption. This solution, resulting in increasing the place-values of the output of distant lands, was a commercial achievement due to the application of science to transportation. The other feature of the problem was that of giving time-values to perishables which could not be consumed in the season of production, but could be carried over into the seasons of least supply. This has been the achievement of the warehouseman, aided by the application of the principles of science to the conditions of this industry.[1]

Thus begins the first and last general investigation of warehousing by the government. Special studies on cold storages, grain elevators, and cotton warehouses have been made, and with special purposes in view. The economic problems connected with warehousing, and particularly the commercial aspects of these problems, have never been thoroughly discussed. The most comprehensive treatment of the subject recently made gives a general survey of types and problems.[2]

It remains yet to be shown how fundamental to modern commercial and industrial development the warehouse has been and is.

Warehousemen generally agree that the industry falls far short of mature development. The remarkable progress in refrigeration, the increased demands for surplus stocks by large scale manufacturing and distributing plants, the need for nation-wide service in handling machine accessories and parts, the greater and greater concentration of population in cities where the family storage room is strictly limited to one or two days' supply, the widening markets demanding the accumulation of goods in vast storehouses in different parts of the world—all of these and other characteristics of modern commerce have brought about a greatly increased development in warehousing of all kinds.

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[1] October, 1903, p. 1035.

[2] *Cf.* Lorain Fortney, *The Warehousing Industry.*

In rural districts storage in some form has long been a familiar problem. Fruits and vegetables have been "banked" in the ground, protected by earth and straw from the frost and wet, or have been placed in a cellar either built beneath the house or as an independent structure. Grain and hay are stored away in barns; machinery in sheds. Nearly all of the problems of warehousing may be found in simple form in the country. This is true of cold storage, too. It is necessary to protect perishable food products from the cold of winter, as well as from the heat of summer. The warmly constructed cellar and the cool spring-house are counterparts.

In towns and cities the warehousing problems grow in proportions and complexity. Demand has grown stronger and stronger for a more definite isolation of the warehousing function. In the great trade centers the amount of storage space has become enormous. The warehouses of Chicago, for instance, other than grain elevators and cold storages, have a total storage space of 4,500,000 square feet. The total capacity of grain elevators is about 45,000,000 bushels. In the great free port of Hamburg there is storage space of approximately 4,663,944 square feet.

The roundabout process in modern industry has made necessary the storing of goods, machines and spare parts. Heavy overhead is present in a plant continuously even though it makes seasonal goods, so that these goods need storage space, awaiting the season of demand. Manufacturers of automobiles must furnish convenient service in accessories and spare parts to all sections of a great market; makers of agricultural implements, like the International Harvester Company, must be able to furnish on telegraphic order any possible part of any machine they put out. The steel mills must accumulate an adequate supply of raw materials and fuel. The mail-order house must have its stores from which to fill orders. Storage touches every phase of industry and commerce. "A definite portion of the resources of civilization is always, so to speak, 'in storage.' "

As soon as a margin appears between production and consumption, the demand for storage or warehousing begins. It aims not only to preserve the accumulations of the past, valuable for record or because of their associations, or for adornment, but also to provide against future want. As industrial society grows more complex, as it develops interdependency, specialization, and systems of exchange, the industrial and commercial needs for storage greatly increase. Learning the lesson from experience and from nature itself, men began to care for surpluses and accumulations. To-day, there is a world-wide warehousing industry, absolutely indispensable for industry, for trade, and for human welfare.

There appear to be three tendencies along which the development of warehousing is now taking place. "In the one case the warehouse would naturally seem to be a commercial institution because of its close connection with trade movements. In the other case the discharge of the duties involved in warehousing is such as to give the establishment a status which is more nearly allied to that of the bank than to that of the mercantile house."[3]

A third tendency is connected with manufacturing rather than with trade and aims at leveling out seasonal industries, at carrying surplus or reserve materials and stocks. The functions performed in each case will be discussed in the following section.

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[3] "Warehousing Industry in the United States," *op cit.*, p. 1088.

**116. Functions of the Warehouse.**—There are many important services which the warehouse performs. Not all of these belong to it as a distinct institution; several, in fact, are performed incidentally to the real business. They are as follows:

(*a*) *Storage.*—The primary function of the warehouse is to save the surplus or reserve of "storable utilities." There are surplus and deficit communities, nations, seasons. It is the duty of the warehouse to accumulate during the flush season or in the surplus community or country, for the purpose of distribution in the season, district or country of scarcity. Economically speaking, the storing of goods is for the purpose of creating time-utilities.

(*b*) *Sharing the Risks.*—The warehouseman, when he receives goods, accepts the responsibility to deliver them in as good condition as he received them. In this way he takes from the owner the risk for the goods in his care while they accumulate time-utilities. While storage is the primary function, under our modern business organization this corollary function is practically forced upon the warehouseman.

(*c*) *Placing Insurance.*—In order to share the above risk with the community, the warehouseman, in turn, takes out an insurance policy against the goods which he receives. Because he has used care in the construction of his warehouse, and because he is especially equipped to look out for them, the rate of insurance is low. Thus, the burden of the risk is not only spread over many people, but also the risk itself is reduced to a minimum.

(*d*) *Financing Depositors.*—The warehouse is a commodity bank. Against the goods credit is granted and thus the owners are financed until the goods are sold. This is a particularly important and a continually increasing service to the small manufacturer, who makes seasonal goods. As they accumulate in the warehouse it is possible for him to draw against them on a warehouse receipt and so finance his plant to run continuously.

(*e*) *Handling and Transfer of Goods.*—It is possible to consign goods to a warehouseman for handling in the trade center and for transferring them either to another transportation line or to the purchaser. These services are also clearly subsidiary to the primary storage function.

(*f*) *Sorting, Packing, Labeling.*—Other incidental services which are frequently performed by the warehouseman are sorting the commodities, packing them for shipment or storage, and placing the proper labels on them.

(*g*) *Cleaning, Drying, Etc.*—In the same category are the cleaning, drying, or other preparation of the goods to make them more readily marketable. The elevator man may fan the chaff or the dampness out of the grain. A great social service was done by the warehousemen in the autumn of 1917 when they received the water-soaked corn from all sections of the corn belt and put it through a drying process, thus making possible the redemption of a part of the food value of that great crop.

(*h*) *Inspection of Goods.*—Receipts cannot be drawn against goods until their character is determined. For this purpose the warehouseman inspects the goods upon arrival, unless they have previously been inspected by a responsible party. To ascertain whether or not the storage man has done his duty in keeping the goods without waste or deterioration, another inspection is necessary upon their delivery.

(*i*) *Exhibition and Selling of Goods.*—A further incidental service performed by warehousemen is the exhibiting and even the selling of goods entrusted to them. A noted example of this service is to be found in the sample rooms of the great Bush Terminal warehouse system.

(*j*) *Support of Auctions and Produce Exchanges.*—Where "spot" sales are made through organized exchanges, the commodities must be at hand for delivery. This means that they must be in an available storage somewhere near the exchange. They may be "on track," that is, stored in a freight car or in a warehouse. At least a temporary storage must be had for goods to be sold at auction. Convenient to auctions, markets, and organized exchanges of all kinds there will be found the necessary warehousing facilities.

(*k*) *Handling Exports and Imports.*—A warehouse system is essential to every great port in the handling of exports and imports. Through these institutions the middlemen in foreign trade work. The commission houses must have ample storage facilities in the home ports and in the foreign ports.

(*l*) *Miscellaneous Services.*—There are other incidental services which the warehouseman performs. He may collect goods into carload lots and become a forwarding agent; he may secure and disseminate market information; he may make purchases for his patrons. Being a business man in a competitive industry, the warehouseman is seeking to attract business, to build up good-will. Whatever he can do to secure this good-will, he is glad to do.

**117. Economic Advantages of the Warehouse.**—The warehousing industry has developed, persists and thrives because of the economic advantages gained through it. Chief of these economic advantages are the following:

1. The warehouse aids in adjusting the supply of commodities to the needs of the community.
2. It encourages the production of perishable products, over and beyond the seasonal demands.
3. It prevents irregularity in manufacturing both by

making possible a reserve store of materials on hand and by affording the basis for credit.

4. It tends to smooth out the production peaks.

5. It aids in adjusting market supply during the season of surplus and of scarcity.

6. It offers a physical support to competitive and speculative industry.

**118. Types of Warehouses.**—There are several distinct types of warehouses, with common functions but classified on the basis of the goods which they handle. Since the point of view here is a commercial one, the storage warehouse that devotes its services to the storing of household goods will not be discussed. Attention has already been called to the fact that the freight car is a movable warehouse and the refrigerator car is a movable cold storage. These need not be further discussed. The railroad freight sheds, the shipping rooms of manufacturing plants and wholesale establishments, are temporary warehouses. They are not, however, of sufficient importance to deserve special attention.

**119. The General Mercantile Warehouse.**—As the volume of business in any line increases there is a tendency toward specialization in warehousing; but where there is not sufficient business to justify specialization and, to some extent, elsewhere the prevailing type is the general mercantile warehouse. It is a warehouse fitted to handle many kinds of commodities and corresponds to the general store. In such a warehouse there may be a hunderd or more different kinds of articles in storage at the same time. These may comprise such widely varying articles as salt, lime, liquor, tobacco from Turkey, tea from China and India, coffee from Brazil, silk goods and gloves from Japan, jewels of an actress, an Egyptian mummy, sugar, flour, hides and leather, ‘‘spices from Araby,’’ and many others.

The general mercantile warehouse must, therefore, be adaptable to caring for many different kinds of goods.

Some of them are perishable and will deteriorate very easily. Many of them cannot be placed together in the same compartment. There is also the question of the quantity of light which is to be permitted to enter; there is the question of humidity of the atmosphere; there is the question of temperature. There is also the problem of keeping records in order that at an instant's notice the manager may report the amount of goods on hand, the character of the goods, by whom sent, and to whom they are to be delivered. He must know, also, the space that is available for storage at all times. He must establish connections so that the goods will come to him for safe-keeping, and he must be ready to accommodate the merchant who may ask for them at any time, and in any quantity. For all these services it is also his duty to set a rate of charge. He must study his business in its broader aspects as to what forces are at work to increase or decrease his usefulness—where he belongs in the scheme of things. This warehouseman, therefore, to meet all his problems, must know something of the physical and chemical sciences, something of mechanical engineering, something of accounting, something of labor management, and in addition he must be a merchant of his services.[4]

Warehousing, so far as the general mercantile warehouse is concerned, develops in importance with the growth of the trade center. On a large scale it is essentially a big-city business. But everywhere along the line, from the origin of materials to their consumption, the general warehouse performs in varying degrees the same functions. Like the common carrier, the public warehouses must in some states serve all who call upon them without favor or discrimination. In Illinois, for instance, they are public utilities and operate under the supervision of the public service commission. They protect, they insure, they bear the risks.

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[4] C. S. Duncan, *Commercial Research*, p. 31.

They are as important to industry as the bank and the railroad. With the growth of industry they become more and more specialized institutions.

**120. The Bonded Warehouse.**—This special type of warehouse arises from the fact that certain revenue taxes are levied by the state on goods of a certain character. In general, the bonded warehouse has to do with the import trade and is best exemplified in the Customs Houses. There are, however, bonded warehouses for domestic trade. This business may be carried on in connection with the general mercantile warehouse, but wherever there is such a warehouse business, it is under the charge and control of Government agents.

The bulk of the commodities in the bonded warehouses has been liquors. Such goods could be put under license and released in the quantities desired, the revenue being paid as they were released. The government allowed eight years for dues to run against liquors. In this way the bonded warehouse becomes the neck of the bottle through which these goods must pass and where they may be most readily controlled.

On the basis of the character of the bonded goods carried, there are three kinds of bonded warehouses. These are distillery warehouses, general bonded warehouses, and special bonded warehouses. They all perform the same kinds of functions.

**121. The Grain Elevator.**—A particular type of warehouse has developed to handle the great grain crops of the country. This type is called an elevator because its construction takes advantage of the flowing quality of grain. The grain is, in fact, elevated from the wagon, the car, or the hold of the ship, to the top of the warehouse and is then permitted to flow or is carried on broad rubber belts to the storage bins.

There are several different types of grain warehouses.

The grain grower has his crib or bin for storing sufficient quantity for feeding and seeding purposes, at least, and often for holding back the supply for a better price. At the local, or country, markets are the small elevators, frequently connected with a local flour mill, and the grain warehouses that are used for a brief period to handle a share of the local crop on a commission basis, to be devoted at other times to housing wool, potatoes, and so forth.

There may be also at important local markets the farmers' elevator, run on a coöperative basis by the grain growers themselves. In this case the producers are absorbing the functions of middlemen. As is well known, this movement for farmers' elevators began in the Granger movement during the '70's, when the grain growers banded together to fight the railroads with their elevator lines. A combination of control of transportation and storage shut the growers out from the markets. Railroads were then declared to be public utilities, and later in certain grain-growing states the elevators were also declared to be public utilities. The farmers' elevators then sprang up and have in recent years made heavy inroads into the grain-storage business.

The so-called "line" elevators were built along the line of a railroad system tapping the grain-producing areas. These elevators led into the terminal elevators at the large market centers. Here they entered into competition with the elevator men already in business. The control of the line elevators was so great, however, that by 1896 the independents were practically frozen out, in Chicago, for example. In consequence, the flood of grain was divided, some flowing past this center, some being diverted to the north through Duluth, some being carried on to the Atlantic coast by the great trunk lines.

The power of the "line" elevators has since been broken and the farmers' elevators have rapidly developed, while the independents have almost held their own. At first the grain elevator business in the local, the primary, and the terminal market was done by independent elevatormen. Usually it was in connection with the commission business.

The relative position of the three main types is shown by the following figures for Minnesota:

| Kind | Number | |
|---|---|---|
| | 1906 | 1910 |
| Line | 1196 | 871 |
| Independent | 381 | 363 |
| Farmers' | 151 | 224 |

In 1913, there were over two thousand coöperative elevators in the United States, which handled 40 per cent of the crop.

Storage is a strategic function in marketing grain. "The key to a proper comprehension of the primary market in the grain distribution lies not in the railway systems nor in the local elevator systems, but in the control and operation of the terminal elevator systems. These elevators are the receiving and storing places for the grain gathered into primary markets through the local line elevators."[5] The grain elevator serves not only to store the grain and to transfer it, but also to clean and to mix it. Herein lies one of the abuses, as will appear in the discussion of grading.

It is possible in certain sections of the country for grain to reach the primary or terminal market without passing through an elevator. This is true in the West where wheat, for instance, when it is threshed, is piled up in the fields in sacks, until the time when it can be shipped. In the marketing of corn throughout the corn belt, the local cribs that used to line the sidetracks at every small station, built to carry the crop locally, so as not to flood the central markets, have disappeared. The vast bulk of this cereal crop is now swallowed up in the elevators of the larger markets. The big flour mills have built their own elevators, as have many of the malting and corn-products concerns.

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[5] Report of the Industrial Commission, 1900, vol. vii, p. 70.

One unique characteristic of grain storage is worth discussion. Wheat, as well as most other grain, loses its identity when it passes into the elevator. When the farmer hauls his grain to the local elevator it is run into a bin with that of many other producers. As it is drawn out there is no means of knowing when any particular lot may be run out. This kind of "commingling" continues throughout the marketing process. "The flour in a loaf of bread may come from many wheat fields."

**122. Cotton Warehouses.**—Attention has been called to the marked tendency toward a one-crop system in the cotton-producing region. This tendency has created an important financing problem, for the cotton grower must be carried throughout the entire year, although his one big crop is marketed practically between August and November. The grower has been obliged to draw against his cotton both while growing and after picking. "In the light of all the facts, it seems reasonable to state that but little cotton would be stored or insured if it were not necessary to do so in order to negotiate loans with cotton as collateral. The banks are entirely willing to advance money on cotton on liberal terms when it is properly stored and insured."[6]

It is clear, therefore, that a well-organized system of cotton warehouses would be a great assistance to all concerned in the marketing of this great staple product. But financing is only one of the functions. There is much waste in the careless methods of handling cotton. It is not always protected from the weather on the plantation and it is not always baled in such a way as to protect it. Cotton is neglected more than any other product.

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[6] U. S. Department of Agriculture, Bulletin No. 216, "Cotton Warehouses," p. 2.

There are different types of cotton warehouses. As in marketing wheat, cotton may be stored locally, at the concentration points, in the terminal markets or by the mills. It has been calculated for 1913 that the 3,485 cotton warehouses had a capacity of 13,742,680 "running" bales and that the cotton mills, 823 in number, had a capacity of 1,295,495 "running" bales, making altogether a total capacity of 15,038,175 bales. In this same year the total production was only 13,982,811 bales. These figures show that there was in existence sufficient storage capacity to more than accommodate at one time the entire crop.

The warehousing system has not been well adjusted to the needs of marketing cotton. "In storage capacity the present cotton warehouses are ample, but these warehouses are poorly distributed. The best warehouses are not available to the farmer. The charges of the others are too high because they must pay a high insurance rate and the cost of handling is necessarily great. Some new standard buildings should be erected, but many of those now in use should be remodeled."[7]

The cotton crop is harvested in three or four months, while it requires at least the twelve months for the mills to consume it. An adequate storage system is therefore absolutely essential to keep the crop from flooding the market and depressing the price unduly. Even though the growers sell it, there must somewhere be sufficient storage space. For the material welfare of the cotton producer the storage system should be available to him. When the cotton leaves his hands, it then becomes an open question whether the mills should have storage space or whether a special middleman class should be maintained for this purpose. "The inauguration of an ample and efficient system of warehouses would mark the beginning of a progressive revolution in the cotton markets."[8] It has been estimated that there is in normal years a loss of from $30,000,000 to $75,000,000 worth of cotton from "country damage."

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[7] *Ibid.*, p. 25.

There are six kinds of cotton warehouses, judged on the basis of the progress of cotton from the field to the mill: (1) on the farm, (2) at the gin, (3) at the concentration point, (4) at the port of export, (5) at the port of import, (6) at the mill. To attract cotton to New Orleans there has been built as a municipal enterprise a great modern cotton warehouse, with all the up-to-date equipment. In consequence, "there is more handling machinery employed, better shed facilities and capacity furnished, greater length of dock frontage available on a deep channel in proportion to import and export tonnage, in the Port of New Orleans than in any other American or foreign port examined."[9]

As was true with wheat, there must be ample warehousing room in connection with cotton exchanges to care for all the "spot" sales that may take place. The amount of cotton passing through the New York exchange is not great, and no extensive storage space is demanded.

**123. Wool Warehouses.**—There is no great central market in the United States for wool. Attempts have been made at times to organize such a market as exists in London. In 1894, the New York Wool Exchange was organized, but it did not succeed. Wool-marketing methods would not adjust themselves to it. More recently warehouses have been built at local concentration points, where the wool may be graded and sold at auction.

Attempts have also been made to establish wool warehouses at large primary markets, such as Chicago and

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[8] U. S. Department of Agriculture, Bulletin No. 277, p. 5.

[9] Von Phul, *Physical Characteristics of Cotton Warehouses*, p. 5.

Omaha. Some of these have been successful; some have not. It has not been possible to make these cities into wool-trading centers. One warehouse lost $50,000 in an attempt and then concluded it was an illogical plan. They can serve, however, as assembling and transfer points.

The most important warehouses are at the "terminal markets," and especially in Boston and Philadelphia. One warehouse in the former city has a storage capacity of more than 100,000,000 pounds. It is in connection with these warehouses that the wool merchants function. They serve as the wholesale wool store for the New England manufacturers. To them the manufacturers can come at any time and secure the amount and the grade of wool required.[10] These warehousemen are generally spoken of as commission men.

**124. Tobacco Warehouses.**—Tobacco is stored immediately upon cutting in "barns" where it is cured. It is then hauled to the local market where it is put into local warehouses. These often have a large open floor where the tobacco auction may be held. From these local markets it is consigned to commission merchants or warehousemen in the large nearby centers, such as Baltimore, Louisville, and Cincinnati. Often six months, a year, or two years elapse after the tobacco has been sold by the producers before it is manufactured. During this period, it must be protected and insured. "The length of time tobacco may remain in storage in the hands of dealers and speculators is entirely problematical and would depend largely on market conditions, but would not generally be for more than a year or two. The more important storage centers for leaf tobacco are Louisville, Cincinnati, St. Louis, Richmond, Baltimore, Durham, and Danville."[11]

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[10] *Cf.* Cherington, *The Wool Industry,* pp. 66-72.

[11] U. S. Department of Agriculture, Report No. 98, "Systems of Marketing Farm Products," p. 160.

Like wool, tobacco is sold on inspection or by special samples. An auction or sales room is, therefore, a necessary appendage to a tobacco warehouse. Here, too, grading, even though crudely done, takes place. Many of the middleman functions are thus concentrated in the hands of the warehouseman. The tobacco warehouse may become as strategic a point in marketing as the wool warehouse.

**125. Cold Storage.**—One of the great modern discoveries is the method of preserving perishable foodstuffs. It has not only relieved the world forever from the fear of actual famine, but also has made possible the enjoyment of many exotic delicacies. The cold storage warehouse has the duty both to protect and to preserve the goods that it receives. Storing of this kind becomes a technical problem; the warehouseman becomes a scientist.

Cold storage is a great and growing business.

> It is difficult to estimate the extent of the cold-storage industry. The best figures obtainable indicate that there are between 700 and 800 public cold storage warehouses in this country, aggregating approximately 200,000,000 cubic feet of space. About 1,320,000 carloads of perishable products pass through the warehouses in the course of a year, valued at approximately $600,000,000. These figures do not include the fresh meat which is refrigerated in the packing houses and public markets, and which amounts to 16,000,000 pounds yearly. We have no figures concerning either the space or the products stored in private houses, of which there are probably 2,000.[12]

Cold storage, in one form or another, extends from the source of perishable products to their consumption. Fruits and vegetables may be canned or "banked" by the housewife, or kept in the cellar on the farm; and they may be preserved in the ice chest by the consumer. All the way along between these two there must be protection and preservation. The carrier has his refrigerator car, or ship, or truck. Perishable products are thus carried to all the chief markets of the world; chilled beef from the United States and Argentina to Europe; bananas from the tropics to all parts of the temperate zone; fresh fruits from the West and South to the Eastern and Northern cities, from the Mediterranean region to far-flung market centers. And in those market centers there are the great cold-storage plants. What other types of warehouses do for other commodities the cold storages do for perishable products, for fruit, vegetables, eggs, butter, meats, etc. They are essential in the distribution of the supply throughout the year and geographically.

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[12] M. E. Pennington, *Annals of the American Academy of Political and Social Science,* vol. xlviii, p. 159.

In the marketing of perishable products the cold-storage warehouses are strategic. They collect the surplus supply during the height of production and distribute it during the period of deficiency. In this period of deficiency the market must look to the cold-storage men and the "commission men" for the supply. These men have, therefore, been accused of manipulating the market. In fact, two complaints have been made against them: (1) that they have filled their storage houses with products bought on a glutted market and have unduly increased the price in the slack season; and (2) that they have put deteriorated goods on the market.

As regards the first complaint, the theory is that, "if a portion of a product is withdrawn from consumption at a time of the year when production is relatively large and released for consumption when production is relatively small the result is that the prices will be raised during the period of natural surplus and depressed during the period of natural scarcity, so that there will be in operation an equalizing force."[13] It was found by investigation, in 1912, that this contention made by cold-storage men that a tendency toward uniformity of prices exists is largely true, but is not true for all commodities going into storage. The effect upon price will vary largely in proportion to the relative amount that goes into storage. It has been calculated that 3.1 per cent of the year's production of fresh beef, 4.1 per cent of mutton, 11.5 per cent of pork, 9.6 per cent of butter, and 15 per cent of eggs, go into storage. On November 16, 1917, the holdings of 275 cold storages were reported as 46,206,059 pounds of frozen poultry. Reports from 266 cold storages for July 15, 1918, showed holdings of 65,874,378 pounds. In all of these products, Government investigation has shown that practically the entire receipts are exhausted within ten months. On February 1, 1916, there were in 416 cold storages 4,363,686 barrels of apples.

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[13] Holmes, *Cold Storage: Business Features,* p. 68.

Statistics show clearly that on the whole the price line is leveled out by cold storage. It is to be remembered, however, that the holding of this reserve supply ready to be let loose upon the market, gives to those who control it a tremendous advantage in case of disaster or misfortune to the new crop. The strategic time in the storage business is the period just preceding the advent of a new crop. Storage charges are running against the goods; most kinds cannot be held over successfully for the second season; the ideal is to clear out the stocks just in time to care for the new supply. It is a matter for nice judgment; it is a matter for speculation, if it does not degenerate into pure gambling. If a substantial portion of the existing supply is destroyed or if the new season opens late, those who control the remaining supply find a seller's market. If the supply is underestimated, it may become a buyers' market. Social control alone can protect the public against profiteering.

As to the deterioration of the products, there has been a basis for complaint. But every business must fight its way up to better methods. The cold-storage business has done this in a most worthy manner. The following may be taken as a fair judgment on the situation: "Current opinion holds that cold-storage warehouses are dirty, unsanitary places. The fact of the case is that they are, almost without exception, far cleaner than the butchers' icebox, and infinitely ahead of the house refrigerator, as commonly kept by the present-day servant."[14]

Cold storage has developed into a new science. From a crude beginning, refrigerating and chilling methods have steadily improved. A refrigerator car was placed in service in 1868. Boston received a consignment of dressed beef in September, 1869. The refrigerating system, both on the railroads and in warehouses, centered in Chicago, which is to-day the chief cold-storage center in the United States. In many instances the refrigerating material is ice, but the modern refrigerated warehouse uses no ice. In them refrigeration is obtained by piping a calcium chloride brine or liquid ammonia. The temperature can be nicely adjusted to obtain the required results. To-day, the most important consideration is to get the perishable products into the storage before they begin to decay.

There is no doubt that cold storage is the most important single factor to-day in the conservation of foodstuffs. The system so beneficent when rightly used should not be permitted to have its power abused. Cold-storage goods must not be sold as "fresh" goods. Regulations are rightly made to compel the labeling of such goods. The tendency is more and more to consider the cold storage as a public utility.

**126. Stockrooms.**—Another feature of warehousing is the carrying of supplies of raw materials and stocks of goods. The question here is whether the individual business shall perform these services for itself or turn them over to the specialized middlemen. The larger firms carry their own supplies and stocks. This applies to merchants as well as manufacturers. A large department store has devoted a large loft-room space to the storage of furs; most large retailers have their neighboring warehouses. The Standard Oil Company has built its own oil tanks. The International Harvester Company has built several large warehouses. One recently constructed in Chicago will permit the storage of 1,500 carloads of goods. It has 3,723,527 cubic feet of space.

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[14] Pennington, *Annals of the American Academy of Political and Social Science,* vol. viii, p. 156.

The requirements of each individual business will determine the warehousing service. A mail-order house will need to have a reserve stock to meet its needs. A department store will have its storage problem; each manufacturing plant will meet the same problem. Some kind of storage will in every instance be necessary.

**127. Warehousing Problems.**—There are three general types of problems that a warehouseman must face: (1) mechanical, (2) commercial, (3) legal. The mechanical problems have to do with the size of structure, the material and the equipment. Rooms have a certain most efficient size and shape. The heat, moisture, and light must be regulated. The strain of the load must be cared for; mechanical devices are needed for handling heavy articles, for lifting and lowering them.

The commercial problems of a warehouseman have to do with an efficient performance of his functions. He must select an economical location, where rent is reasonable, where transportation is available, where insurance risks are low, and where contact may be had with patrons. In other words, the warehouseman must meet competition and must sell his services as a merchant sells his wares.

The relation of a warehouseman to his patrons is contractual. This contract originates in the acceptance of the goods for storage and in the warehouse receipt. Under these conditions the obligation of the storage man is to receive and store the goods, to exercise ordinary care in keeping them safely, to afford the depositor ready access to the goods, to deliver the goods in accordance with the contract and provisions of the law, and to undertake such additional responsibilities as are created by special contract. The care required is such as a reasonably careful owner of similar goods would exercise. A warehouseman is not responsible for losses due to an act of God, to a public enemy, to defects inherent in the goods stored, or to other causes not due to neglect.

The identity of some goods must be maintained, but not of others. The latter are fungible goods, where the units are so alike as to become interchangeable, such as grain and cotton. The former are non-fungible goods. A warehouseman has a lien against the goods in his care for storage charges only, and then but from the date of receipt. Other charges must be stipulated, for interest, insurance, transportation, weighing, etc. These are enforceable against all goods. But the right is lost by the surrender of the warehouse receipt.

**128. Place of Warehouse in Commercial Organization.**—The preceding discussion demonstrates the fact that the warehouse is as important in modern trade as the railroad or the bank. Indeed, the warehouse is to storable commodities what the bank is to money. It is a safe depository; it carries a reserve to guard against want and famine. "The inflow and the outflow of the volume of storage business is one of the best indexes of the degree of business prosperity." So essential for the general welfare is the proper functioning of the warehouse system that special laws have been passed to regulate it, as is true of public utilities and banks.[15] It is a materialization of the spirit of thrift and foresight among a people. "The normal place of warehousing in our economic system seems to be determined by these four relationships—with the transporter, with the merchant, with the manufacturer, and with the banker."

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[15] *Cf.* U. S. Warehouse Act, August 11, 1916. The Cotton Futures Act, etc.

### SUGGESTIONS FOR STUDY

The student should now study the warehouse in relation to his chosen commodity. The classroom work may be based upon the following topics:

1. Tidal movements of stored goods.
2. Effective reserve of goods.
3. Location problem of a warehouse.
4. Scientific aspects of warehousing.
5. Control of warehousing.
6. Percentage of total supply in storage.
7. Control of goods in storage.
8. Social problem in cold storage.
9. Historical development of warehousing.
10. Warehousing in relation to middlemen.

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# CHAPTER IX

## COMMERCIAL GRADING OF COMMODITIES

**129. The Need of Uniform Standards.**—Commercial dealings in goods of every character demand some sort of a unit as a basis. Money is used as a medium of exchange because it has become a common standard of value, a universally applicable measuring rod. Men think of economic goods in terms of quantity or quality and unless these terms are the same the parties to a trade can have no meeting of minds. Practically, there are no goods on the market that do not run on some standard or grade.

"There are, in general, two classes of units that may be used. There is, first, the unit of individual things. This is determined by counting the actual number of individual things in a group. There are, for example, so many bushels of grain, so many yards of cloth, so many dollars in money, or so many pounds in weight. The other kind of unit is called the measurable unit and is to be applied to the quantity without regard to the individuality. There is, for example, the length or the capacity of a container."[1] It is clear that a mere number applied to a commodity will mean nothing in commerce unless the units so numbered are understood. Many of our commercial units are arbitrary and the result of accepted convention. In the United States men speak of the foot, the yard, the mile; in Europe many people use meters and kilometers. Pounds may be used here; kilograms there. In this regard, however, the kind of unit does not matter greatly if only it be serviceable and understood.

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[1] C. S. Duncan, *Commercial Research*, p. 19.

In order that commodities may be classified on the basis of some unit there is need of inspection, of weighing, of sampling, or of some other method of establishing a grade. The purpose of the whole process is standardization, and the object of standardization is to be able to deal with commodities in the mass.

**130. Commercial Function of Grading.**—In marketing there has been a constantly increasing need for standard grades. This demand has developed with the growth and widening of markets. When the bulk of transactions takes place in goods not seen by both parties, some kind of grades are essential. "Long range" selling of every kind would become a pure gamble otherwise. Money is a universally acceptable commodity because it is based upon a common, known, and rigidly enforced standard. Every one can know what he is getting. Commercial grading of goods is necessary in order that the buyer at long range may know what he is getting.

If one is able to deal with commodities in the mass rather than individually, sales may then be on the basis of samples. The selling by sample saves the expense, time, and trouble of inspecting each unit. In raw materials and foodstuffs, however, some one must at some time make an inspection of each unit. Nature works according to laws, but the natural resources are not found standardized. Herein lies a fundamental difference between raw materials and foodstuffs, and manufactured goods. With standardized materials a machine process of manufacture may be started that will produce any number of units "just alike." The constant problem of standardization exists in the materials.

By proper grading it may become possible also to sell by description. This is true to-day of goods sold through advertising. A great amount of time and expense could be saved if sales could be made satisfactorily on the basis of description.

Of more importance is the relation of grading to future contracts. It would be impossible for organized exchanges to deal in "futures" without a thorough grading system. In fact, difficulty has arisen recently both on the grain exchanges and on the cotton exchanges in regard to standards and methods of grading. Every commodity that can run satisfactorily on standard grades, can be traded in on the exchange.

In the local market, where commodities are small in quantity and it is not difficult to inspect each consignment, grading is not of so great importance as elsewhere. Nevertheless, even there grades will be found, even though goods are traded in by guess. Scales are used now practically everywhere to establish the standard pound; yardsticks are used instead of measuring from tip of nose to elbow; eggs are sold by "count"; coal by the ton; grain by the bushel; wood by the cord; hay by the "load" or the ton. Rough and ready standards may be used, but units of some sort are essential. Even in the local market much in the way of improvement needs to be done. Wheat has graded higher on the average in the primary market than in the local markets. This is an injustice to the producer. An improved grading system would be of special value to the producer of farm products.

Take the case of cotton. Producers have been compelled to sell practically all of their cotton on the "middling" grade or lower. "For his best cotton he (the producer) may get 'strict middling,' but rarely anything higher. Experience soon gives the buyer a knowledge of grade and staple, which the grower can never acquire in equal detail. The latter is practically compelled to sell his product on a quality basis specified by the person who is purchasing it. The farmer must either know more about grade and staple, or he, collectively as a community, must have some one in his employ who will put him in a position to trade as other people trade in their products."[2]

The situation holds true, to a greater or less extent, for all commodities. A theoretically fair bargain assumes an equal knowledge of grades on each side.

In the broader market, grading becomes even more essential. The primary market, the wholesale trade, the national and international markets are moving toward scientific grading of all commodities. Goods must be bought and sold here by grade, by sample, by description.

The consumer is likewise interested in grading. Standardization may be the consumer's safeguard; it may also weaken his defense. When goods run on grades, the consumer has a background of experience upon which to form his judgment in making purchases. On the other hand, he may come to rely upon standards and grades and lose his power of discrimination. Under a system of *caveat emptor,* the buyer can beware only when he is trained in defense. Higgling in the market trains the buyer in judging quality. The average buyer to-day, who makes purchases by name or trade-mark or on the advice of the retailer, has no such judgment.

In regard to some goods, the determination of quality is a technical problem. The average purchaser does not possess such knowledge. If adulteration or deterioration becomes detrimental to public health, the question of maintaining standards is a social one. It is for this reason that the Pure Food and Drug Act was passed in 1906. In this place also belongs the law of July 24, 1919, which instructs the Department of Agriculture "to investigate and to certify to shippers and other interested parties the quality and condition of fruits, vegetables, poultry, butter, hay, and other perishable farm products, when received in interstate commerce.'' Such independent inspection and certification would have averted the suspicion that attaches to the commission merchant who deals in perishable products. It will doubtless tone up the business from producer to retailer.

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[2] Brand, *Improved Methods of Handling and Marketing Cotton,* p. 455.

The problem of grading is related to the problem of financing the marketing. It is unsatisfactory for any middleman to be ignorant of the grades of goods which he handles. His liabilities may prove to be unfairly large or he may escape his full responsibility. But more important is the fact that no one will loan money against goods of unknown quality, except at a high rate. Even then it is not a sound commercial policy. For the proper functioning of the warehouse receipt, the trade acceptance and the bill of lading, goods must be carefully graded.

**131. Scientific Analysis as a Basis for Grading.**—More and more clearly business men are coming to see that by means of weighing, inspecting, and testing, commodities must be classified according to grades. In times past the grades have been too loosely constructed. Cotton, for instance, may be upland or Sea-Island, long staple or short staple; wheat may be winter wheat or spring wheat, hard wheat or soft wheat, or ''Smooth Velvet,'' ''Mediterranean,'' ''Durum,'' bearded, or what not; potatoes may be ''Early Rose'' or ''late white''; apples may be graded on the basis of geographical location of productive area, or by botanical name. These are not really commercial grades.

It may be pointed out in this place that there is an essential distinction between species, genera, and common or even trade names, on the one hand, and commercial grades on the other. The principle must be applied here that was applied in the classification of commodities for the purpose of setting transportation rates. The Interstate Commerce Commission said that classification must be based upon those qualities and characteristics that affected the actual transportation. The principle in commercial grading is that grades must be established upon the basis of utilities, the want-satisfying qualities when applied to a particular use. In the application of this principle science may be an indispensable aid.

It does not make much difference what kind of a name is applied to grades established in this way, provided only that the buyer and seller may be assured that the name stands for certain characteristics and qualities.

The manufacturer buys wool or cotton to make a certain kind of cloth. If he buys by grade he must know what the grades stand for in relation to the cloth-making qualities of the raw material. In the careless method of business, in some outlying districts, a cow is a cow and nothing more, except possibly as to color and weight. But a Guernsey is more than a mere cow. Eggs are still bought often "by count"—so much per dozen regardless of size or condition. The introduction of candling methods is modifying this. The main point is that goods are bought to satisfy certain wants; if they are bought at long range, there must be grades that express the want-satisfying qualities.

In order to determine these qualities with accuracy, scientific tests may be made. Industrial chemistry has been developed for this purpose. The U. S. Bureau of Standards is constantly busied with this problem. Industrial plants have their testing rooms and methods. Gradually the analysis of products with that purpose in view for which they are to be used is being refined and made more scientific.

**132. Machinery for Grading.**—Different kinds of machinery are employed for grading commodities and for setting standards and units. The simplest process is that of inspection. An expert cattle buyer may appear merely to glance at a drove of cattle before he makes his offer. This method requires no machinery. For testing the moisture in corn there has been devised a special machine. Apples, potatoes, oranges may be rolled down a board with holes of a certain size in it. Fruit may be analyzed for its acidity in a laboratory. A large mail-order house has a special laboratory equipment for testing the goods that it handles. Special tests are made under varying conditions for determining the spinning qualities of cotton. A "conditioning house," after the Bradford plan, may be established for ascertaining invariable standards of wool. Ores may be analyzed chemically; wood may be standardized by fiber tests, or by "density rule."

In every case the character of the machinery required will differ. The curious long-handled gauge, the probe, or "trier," used in testing or sampling a car of wheat is for that purpose alone. The elaborate apparatus used by a corn-products company is wholly different. In one case it may be expensive; in another not. It is to be remembered in each instance that the purpose in view is to make an analysis or a test of the commodity as regards the special use to which it is to be devoted. For dealings on an exchange the grading of wheat is not the same as the analysis by a flour miller. The purposes are not the same.

**133. Commercial Units and Standards.**—The units in commerce develop gradually by usage; and even more gradually are these units standardized. In weight, the usage in the United States is the ounce, pound, ton. Abroad, the metric system is used. Great Britain, as individualistic in this as in everything else, clings to an obsolete usage; wheat is sold by the quarter, the hundredweight is 112 pounds, the ton, 2,240 pounds. There are no accurate international grade standards for commodities. The nearest approach to them is in wheat and cotton.

Each commodity is bought and sold on the basis of some unit. Grain is measured by the bushel; coal, ore, hay, by the ton; salt by the barrel or sack; eggs by the dozen or case; livestock by the head; tea by the box or chest; tobacco by the hogshead or pound; cotton by the bale, round or square; fruit by the case or box or crate; milk by the bottle, pint, quart, gallon, or 100 pounds; butter by the pound or tub. Thus it runs through the entire list. Commodities are dealt in on the basis of certain, accepted, and well-known-to-the-trade units that have to do with general physical qualities. On this basis, too, there is an approach to standardization; sufficiently so at least to make trading intelligible.

There is another kind of unit, or standard, by which to judge commodities. This test is the suitability of a commodity for a particular service. Physical measurements, or units, of weight, of size, of bulk, are not enough. In fact the establishing of true commercial grades demands more scientific analysis than these. It is the movement for thoroughly scientific grading that is most significant. It is proposed here to examine several commodities from this point of view.

**134. Wheat.**—An act was passed on August 11, 1916, called the United States Grain Standards Act, which authorized the Secretary of Agriculture to "investigate the handling, grading, and transportation of grain and to fix and establish as soon as may be after the enactment hereof standards of quality and condition for corn (maize), wheat, rye, oats, barley, flaxseed, and such other grains as in his judgment the usages of the trade may warrant and permit" (Sec. 2).

As a result of this act, a careful investigation was made, and on March 31, 1917, the official grain standards for wheat were established. To reach these standards, the grain must be free from dockage, that is, free from sand, dirt, weed seeds, weed stems, chaff, straw, grain other than wheat, and any other foreign material, which can be removed readily from the wheat by the use of appropriate sieves, etc. This dockage is to be calculated in terms of percentage of total weight. If the grain, when freed from dockage, contains more than 6 per cent of grain of another kind it cannot be classed as wheat.

All wheat was divided into six classes, as follows: I. Hard Red Spring; II. Common and Red Durum; III. Hard Red Winter; IV. Soft Red Winter; V. Common White; VI. White Club. Each general class is subdivided and each subclass is graded into number 1, number 2, number 3, and so forth. The following examples will illustrate the subdivision of a main class and the grading of a subdivision:

### CLASS I.

#### *Hard Red Spring*

This class shall include all varieties of hard red spring wheat, but shall not include more than ten per centum of other wheat or wheats. This class shall be divided into four subclasses as follows:

#### *Dark Northern Spring*

This subclass shall include wheat of the class Hard Red Spring of which eighty-five per centum or more consists of dark, hard, and vitreous kernels, but shall not contain more than ten per centum of wheat of the variety Humpback.

#### *Northern Spring*

This subclass shall include wheat of the class Hard Red Spring of which less than eighty-five per centum and more than twenty-five per centum consists of dark, hard, and vitreous kernels, but shall not contain more than ten per centum of wheat of the variety Humpback.

### *Red Spring*

This subclass shall include wheat of the class Hard Red Spring which consists of kernels of yellow or mottled appearance, or of starchy texture, and of not more than twenty-five per centum of dark, hard, and vitreous kernels, but shall not contain more than ten per centum of wheat of the variety Humpback.

### *Red Spring Humpback*

This subclass shall include wheat of the class Hard Red Spring of which more than ten per centum consists of wheat of the variety Humpback.[3]

Sec. 13. *Grades for Hard Red Spring Wheat.*—The subclasses Dark Northern Spring, Northern Spring, Red Spring, and Red Spring Humpback wheat shall be divided into six grades for each subclass, the designations and requirements of which, respectively, shall be as specified in this section.

No. 1 Dark Northern Spring, No. 1 Northern Spring, and No. 1 Red Spring, each, (a) shall be bright, cool and sweet; (b) shall contain not more than two per centum of wheat of the variety Humpback and of wheat of other classes, which two per centum may include not more than one per centum of Common White, White Club, or Common and Red Durum wheat, either singly or in any combination; (c) shall contain not more than thirteen and one-half per centum of moisture; (d) shall have a test weight per bushel of at least fifty-nine pounds; (e) shall contain not more than one per centum of damaged kernels and no heat damaged kernels; and (f) shall contain not more than five-tenths of one per centum of inseparable foreign material, which may include not more than one-fourth of one per centum of kinghead, corn cockle, vetch, darnel, or wild rose, either singly or in any combination.[4]

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[3] U. S. Department of Agriculture, Service and Regulatory Announcements, No. 22, p. 3.

[4] *Ibid.*, p. 7.

Wheat is not all inspected; it is sampled. The samples, however, must be secured according to detailed instructions. In case of disputes, for example, the sample must be at least two quarts in size with approximately one and one-eighth pints in an airtight container, obtained by at least five probes in the car or wagon, or boat, or from sacks at the discretion of inspector, with special samples for bad spots. Special moisture testers, grain sieves, balances, pans, probes or "triers," and containers are recommended.

By this means, common standards are being set up for all parts of the country. In the international market, also, the same standards are making their way. Grain exchanges have greatly aided in this work. The Chicago Board of Trade has gained a world-wide reputation for maintaining fair and accurate grades.

**135. Corn.**—The main standard classes for corn, three in number, are based on color. They are: white, yellow, and mixed. White corn is to consist of at least 98 per cent by weight of white kernels. "A slight tinge of light straw color or of pink on kernels of corn otherwise white shall not affect their classification as white corn." Yellow corn is to consist of corn that has at least 95 per cent, by weight, of yellow kernels. "A slight tinge of red on kernels of corn otherwise yellow shall not affect their classification as yellow corn." Mixed corn is made up of a combination of white and yellow and of other colors. "White capped yellow kernels shall be classified as mixed corn."

Each class is graded into seven grades, numbered 1 to 7. "No. 1, white, yellow and mixed, each, (a) shall be cool and sweet, (b) shall have a test weight per bushel of at least fifty-five pounds, (c) may contain not more than fourteen per centum of moisture, (d) may contain not more than two per centum of foreign material or cracked corn, and (e) may contain not more than two per centum of damaged corn and no heat-damaged kernels."

It is interesting to note this relation of color to quality. The first test of corn is color; the second is moisture, then weight and then follows an examination of other characteristics. From first to last, however, the aim is to judge this commodity on the basis of qualities fitted to satisfy certain wants.

**136. Cotton.**—As has been pointed out previously, the cotton exchanges failed to function correctly, due to faulty grading and correlative causes. The U. S. Department of Agriculture, in 1909, established the official cotton grades, but these have not been universally accepted.

> Several different standards are now in use. These are usually referred to by the names of the exchanges which promulgate them, as the Liverpool grades, New York grades, Augusta grades, etc. The "middling" of one market is not the same as that of another, and likewise with other grades. Identical names are applied in different markets to cotton that differs in quality, value and price. The national standards were prepared to remedy this condition. Nine official grades are recognized, as follows: Middling fair, strict good middling, good middling, strict middling, middling, strict low middling, low middling, strict good ordinary, and good ordinary. The grades designated by the prefix "strict" are known in the trade as half grades.[5]

It is clear that such grading must be made by inspection, and that at best it is vague. The usual method is to grade by the bale. A bale is torn in the bagging and the hand is thrust in, seizes a handful of cotton and draws it out. This process may be followed at two or more parts of the bale. The entire bulk of cotton is thus judged, and on grades thus established cotton is traded in on the exchanges.

This method of grading has been inadequate. The quality of cotton is affected by (a) the time of ripening, (b) the time of harvesting, (c) methods of picking, (d) soil conditions, (e) storms, (f) frosts, etc. The grading factors are: (1) color, (2) relative freedom from leaf or other foreign substance, (3) character. Commercial grades, however, have not considered the fundamental test of all textiles. This is the spinning test. The Department of Agriculture has made comparative spinning tests of Arizona-Egyptian cotton with Sea-Island and Sahalleradis Egyptian cottons. Tensile strength comparisons, bleaching, dyeing, and mercerizing comparative tests were made; likewise, relative length of stable, pliability, cling, and evenness. Obviously, these are scientific tests that apply to the uses of cotton and furnish the true basis of grades. As a result of these tests, the official standards have been set and accurate samples of each standard are now in the hands of all cotton exchanges, and four sets have been locked in steel vaults for safe keeping. This method compares favorably with the Bradford wool tests.

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[5] "Handling and Marketing Cotton," *Yearbook of the Department of Agriculture,* 1912, p. 455.

There is a movement on foot to make the standard grades international. This was proposed at an International Cotton Congress in 1907. No progress was made, however, until June, 1913, when representatives of the cotton exchanges at Liverpool, Havre, and Bremen, and of the leading American exchanges met in Liverpool and adopted the so-called International Standards. But the Americans did not bind themselves to this decison, unless they were adopted by the Department of Agriculture. In 1914, the Department undertook to set up independent standards, and it was decided to be undesirable to follow the International Standards. A universal set of standards would be a consummation greatly to be desired.

**137. Potatoes.**—The Bureau of Markets of the U. S. Department of Agriculture, by investigation and demonstration, established the practicability of reducing potatoes to commercial grades. Field tests were made in the grading and packing of potatoes and their marketing by grade as compared with the ungraded. As a result of the experience the Department of Agriculture has recommended the following grades:

### *U. S. Grade No. 1*

This grade shall consist of sound potatoes of similar varietal characteristics, which are practically free (a) from dirt or other foreign matter, frost injury, sunburn, second growth, cuts, scab, blight, dry rot, and damage caused by disease, insects, or mechanical means. The minimum diameter, (b) of potatoes of the round varieties shall be one and seven-eighths (1⅞) inches, and of potatoes of the long varieties one and three-fourths (1¾) inches. In order to allow for variations incident to commercial grading and handling, five per centum by weight of any lot may be under the prescribed size, and, in addition, three per centum by weight of any such lot may be below the remaining requirements of this grade.

### *U. S. Grade No. 2*

This grade shall consist of potatoes of similar varietal characteristics, which are practically free (a) from frost injury and decay, and which are free from serious damage, (c) caused by dirt or other foreign matter, sunburn, second growth, cuts, scab, blight, dry rot, or other disease, insects, or mechanical means. The minimum diameter (b) shall be one and one-half (1½) inches. In order to allow for variations incident to commercial grading and handling, five per centum by weight of any lot may be under the prescribed size, and, in addition, five per centum by weight of any such lot may be below the remaining requirements of this grade.

### *Explanations of Grade Requirements*

(a) "Practically free" means that the appearance shall not be injured to an extent readily apparent upon casual examination, and that any damage from the causes mentioned can be removed by the ordinary processes of paring without appreciable increase in waste over that which would occur if the potato were perfect. Loss of the outer skin (epidermis) only shall not be considered as an injury to the appearance.

(b) "Diameter" means the greatest dimension at right angles to the longitudinal axis.

(c) "Free from serious damage" means that the appearance shall not be injured to the extent of more than twenty per centum of the surface, and that any damage from the causes mentioned can be removed by the ordinary processes of paring without increase of more than ten per centum by weight over that which would occur if the potatoes were perfect.

The crudeness of this method of grading is obvious. It is apparent, too, that these two grades were not intended to be accepted by the wholesaler and retailer. Much more must yet be done before lasting grades are established.

**138. Hides and Skins.**—As might be expected beforehand, the grading of hides and skins bought in the country is very indefinite. The producer is usually unable to distinguish between grades. There has developed as a working basis a system of grading by geographical sections. The buyers have divided the United States into nine sections and have made price differentials on these sections for similar weights and classes. "It is asserted that the conditions which produce these differences on which the resulting price differentials are based are noticeable especially in the grain, texture, thickness, spread, and quality of the leather, and that they are caused largely by climatic conditions, methods of handling cattle, kinds of cattle, kinds of feed, methods of feeding, ticks, grubs, brands, environment, and the methods employed in skinning, curing, and marketing the hides."[6]

If the geographical sections enable the putting of hides and skins into grades on the basis of the qualities indicated, the means is a reasonable one. The grain, texture, thickness, spread, and quality of leather are certainly essential to the establishing of true grades.

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[6] U. S. Department of Agriculture, Farmer's Bulletin No. 1055, p. 43.

**139. Lumber.**—To standardize the output of Southern Yellow Pine the Southern Pine Association has adopted a set of standard specifications.

> Fully 90 per cent of the output of Southern Yellow Pine lumber in the States named (Texas, Arkansas, Missouri, Louisiana, Mississippi, Alabama, Georgia, and Florida) is graded and classified according to the Standard Specifications of the Southern Pine Association. . . . Quotations of prices are usually made upon the basis of these Grading Rules, which in all essential features have been recognized by the lumber trade for many years.
>
> Buyers of Southern Pine lumber are respectfully requested to familiarize themselves with these in order that they may know what they are contracting for when placing orders, and to serve as a guide in determining whether lumber received is in accordance with the grade ordered.[7]

The general commercial grades of common lumber are determined by inspection. The "recognized defects in Yellow Pine are knots, knot holes, splits (either from seasoning, ring hearts, or rough handling), shake, wane, red heart, pith, rot, rotten streaks, worm holes, pitch, pitch pockets, torn grain, loosened grain, seasoning checks, sap stains, crooks and defects caused by manufacturing."[8] Clearly these defects affect the qualities of lumber in relation to its use. However loosely constructed the grades are, they are placed on the proper basis.

There has long been an interest in establishing lumber grades. In 1909 the American Society for Testing Materials proposed that the grades should be based on the number of rings per inch. Although this system was widely used, it was too indefinite to be satisfactory. The Forest Service, after a careful study of all kinds of trees, presented a new method of grading, known as the "density rule," which was adopted in August, 1915. This rule provides for two classes, the Dense and the Sound. The first class is determined by careful requirements and by accurate measurements, "Variation in the individual character of different pieces of timber is responsible for the difference in strength. Structurally, some are much stronger than others." Upon this essential quality the grades are founded. It furnishes an interesting attempt to reduce a difficult commodity to scientific standards.

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[7] Standard Specifications, preface.

[8] *Ibid.*, p. 7.

**140. Apples.**—Broad classes in the apple trade are made on the character of the packing. Some cities are known as boxed-apple markets, some as barreled-apple markets, and others as bulk-apple markets. Clearly, these are not in reality grades. There is a law, mandatory in some states, which provides for four grades, "Fancy," "A grade," "B grade," and "Unclassified." There is an obvious attempt to relate grades to qualities in this system. It is unfortunate, however, to have laws establishing diverse grades throughout the country. Standardization on the basis of scientific grades in all market centers is highly desirable for every kind of commodity.

**141. Tendency to Grading and Effect on Commodity.**—Whatever the character of the commodity, as it finds its way into market it will begin to develop classes and grades. These may have for their foundation the botanical divisions, but this will be true only where the qualities affecting the utility differ in accordance with the botanical classes. Commercial grades tend inevitably toward this basis of quality. The quality demanded in ores may be purity, freedom from dross or foreign substances. Required standards of purity are secured through chemical processes. Furs may be graded by kinds on the basis of appearance and durability. Milk is graded on the percentage of butter fat that it contains; Chicago by ordinance requires 3.5 per cent. Tea, coffee, tobacco may have flavor as the foundation of grades. Attempts have been made to grade oranges according to the amount of acidity as well as by size.

There are several methods of arriving at commercial grades. Livestock to be butchered is inspected individually and its meat-producing qualities judged. A great number of raw materials and foodstuffs must be so inspected. In addition to inspection the commodities may need to be weighed. One test for corn grades is so many pounds per bushel. And even in addition to the grading, the commodities may need weighing to determine commercial units. The two things must go together—standards and units—before intelligent marketing can be carried on. The commercial units may need to be measured instead of being weighed. A law was passed August 31, 1916, entitled the United States Standard Container Act, which defines definitely the standards in cubic inches for baskets to be filled with grapes, fruit, and vegetables. A table of the "variations" and "tolerances" permitted is also given. The law went into effect November 1, 1917. More refined grades are determined by scientific analysis.

There is no doubt that the insistence upon more careful grading has benefited the producer materially. Not only has he become a more intelligent salesman, but he also has given much more care to the commodities, in culture, in handling, in packing. It has been a severe but wholesome lesson to teach the producers of perishable products that methods of refrigeration cannot undo the evils of carelessness previous to storage. Grading has toned up commodities all along the line. It has made possible the "fancy" goods, at the same time that it has raised the standard of the lowest grades. Better goods flow to market on grade than without grade.

**142. Effects Upon Trade Organization.**—There is a wholesome effect also upon the middleman. The honest men are defended from the rogues. The reputation of all dealers suffers when false measures are found in the market. It is possible to buy more intelligently and confidently at long range. Thus the limits of the market can be extended. Organized exchanges are made possible; future contracts that run "on grade" call forth the specialized middleman to take the risks. As better marketing methods develop there is a beneficial reflex upon business men. "More intelligent business is better business."

**143. Grades and Prices.**—There is a definite relation between grades and prices, as there should be. A standard grade not only fosters more intelligent trading, but also furnishes a basis for standard prices. Future contracts are made on a basic grade, say, "middling" grade of cotton, No. 1 Northern Spring grade of wheat. This does not mean that these grades will be delivered on the contract, but that the price quoted will be in terms of this grade. Then, if other grades are delivered, price adjustments will be made for grades above and below, usually at a fixed differential in price. Before the official wheat standards were set, prices for the same commercial grade varied from four or five cents to seventeen cents per bushel.

Each organized exchange adopts regulations determining the deliverable grades and agrees upon the price differences. In the case of cotton these differences are "commercial differences," that is, differences determined by actual transactions in the market. But quite apart from these established margins, a basic grade aids in stabilizing prices. This grade is like the surveyor's corner stone, always a point of departure, always something to return to for comparison. Inspection and grading greatly facilitate the quotation and publication of "spot," as well as future, prices.

**144. Responsibility for Standard Grades.**—Until recently the organized exchange has been most constructive in establishing grades. This institution found it necessary for its own proper functioning to deal on grades. These, too, had to be carefully determined and rigidly maintained for its own protection. Thus, the Chicago Board of Trade has a world-wide reputation for maintaining accurate standards. Lately, however, the Federal Government has taken the matter up and has defined the official standards for wheat, corn, cotton, and is engaged in the laudable task of directing the marketing of many other commodities by grade. There is no reason why the government and private industry should not coöperate in this work. In certain commodities where adulteration becomes a menace to public health, the responsibility is directly on the government to set and maintain the necessary standards.

It was this responsibility on government that brought into being the Pure Food and Drug Act of 1906, that created an Inspection Bureau for foodstuffs during the war. Laws are becoming more and more strict about the cold storage of perishable products. Eggs, butter, poultry, meats, that have become unhealthful must not be sold in the markets. Thus, the *caveat emptor* principle fades away and governmental control emerges.

The producer can gain for his own products not only a touch of individuality but also a premium as to price by special care in grading his products. Thus, Western fruit carries a premium in the Chicago market over Michigan fruit, because of greater scrupulousness in grading and packing. A grade is not established by the top layer, but by the poorest quality. When a carload of grain is inspected, samples are taken from various parts of the car, and these different samples together establish the grade. If the samples show a layer of good wheat on top and a poor grade below, the entire lot goes at the rating of the latter. The producer who tries in this way to deceive the dealer is only deceiving himself. One act of this sort may tarnish an otherwise unblemished reputation. There is an inescapable responsibility on the producer for fair dealing.

**145. Grading and Packing.**—The reduction of commodities to standard units touches also the problem of packing. In foreign trade this has become a vital issue, but even in domestic trade it has been an important subject much neglected. Goods should, of course, be so packed as not to lose their original grading. Further than this, there is science in the packing itself. At the University of Wisconsin a study has been made of this subject, and principles are being evolved. Efficiency in loading cars and ships, strength to withstand pressure, economy of space within the box itself, convenience in handling, as well as adapting the packing to the character of the commodity, length of journey, and means of transportation, are all involved.

### SUGGESTIONS FOR STUDY

The student should here study the problem of commercial grading as it applies to the special commodity which he has under investigation. The topics given below may be made the basis of further study in which the readings that follow will be of great assistance:

1. Definition of a standard grade, a basic grade.
2. Governmental establishment and maintenance of grades.
3. Laboratory experiments to set grades in perishable products.
4. Determining the basic qualities for grades.
5. Standard grades and prices.
6. Standard grades and speculation.
7. Uniform standards of grading.
8. Standard grades in relation to "hedging."

9. Grading of materials and manufactured products.
10. Mixing grades in storage.
11. Grading function in relation to middleman.
12. Width of grades.
13. Grade steps: how determined.
14. Definite limits to grades.
15. Possibilities of scientific grading.

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# CHAPTER X

## TRADE INFORMATION

An ingenious Englishman presented a paper, copiously illustrated, before the Royal Society of Science in 1699, dealing with a new invention which he had just made. This invention was a huge megaphone, or "speaking trumpet," set up on standards, and it was devised for the purpose of communicating at great distances. A sovereign, it was claimed, could stand on some promontory in the midst of his realm and send his voice to its farthest corner; he could stand on the shore and command his ships far out at sea; he could issue proclamations and control activities of peace as well as give orders to his vast armies in times of war. News of disaster or success could be conveyed instantly from one section of the country to another. In fact, the "stentorophone," as it was called, was to become an instrument for making possible an instantaneous transmission of news.

The "stentorophone" would not work, of course, but its inventor had undoubtedly caught a glimpse of the significance of a great idea—that information, knowledge, news, is a vital element in both peace and war. In no part of human activity is this element of information more important than the economic, and especially in that most sensitive of all economic mechanisms, the market. There knowledge is literally power. Market news is the nervous system of the market.

**146. What Is Trade Information?**—"All news is market news," said one of the leading crop experts of the country.

Whatever has any effect upon the market price is trade information. This means that any event which changes in any respect the supply of or demand for any commodity is market news. The event does not need to be economic in character; it may be the election of a senator or a President; it may be a political or a social event abroad. Whatever influences trade and trade relationships is market news. But such event is not really in itself market news; it becomes so as it passes through the mind of the business man, where it is transmuted from an historical incident into trade information. The facts are the raw materials; the business man's interpretation of them is the market news. For market news is nothing more than the reports of events and happenings of the world acted upon by a trained and experienced business mind.

Of market news, time is the essence. For, in the bargaining process superior knowledge may be secured in two ways; it may be a broader, sounder, more comprehensive knowledge, or it may be an earlier knowledge. As a market becomes more and more thoroughly organized, competition in knowledge tends to be narrowed to securing an earlier knowledge. A marvelously efficient organization has been developed as a result of this sort of rivalry, and has concentrated itself in the organized exchanges. As has been shown already, the activity most frequently associated with organized exchanges is dealing in "futures," and to deal intelligently there must be a broad and sound basis of knowledge. The very sensitiveness of exchange prices is due to their immediate response to market news.

The facts secured from all parts of the world by the exchange brokers pass through the minds of these seasoned and expert traders and are there transmuted into market news. A drought in Argentina, a flood in China, a volcanic eruption in the Antipodes, will be instantly translated into dollars and cents in the prices of commodities.

Knowledge of facts, then, that can be judged on a price basis is market information.

**147. Function of Market News.**—The physical world turns on its axis. The ancient mind conceived of it as being pivoted on the shoulders of a giant, Atlas. It is a "going concern," whose activities are adjusted by certain forces. There is a loose analogy here with the world of business. It, too, is a "going concern." Like the physical world, it turns on its axis and pivots on the shoulders of its Atlas. The pivot and the axis of the business is price; and the essence of price is market news.

Practically, the consumer usually pays the price that is asked by the seller in the retail trade. He does not know enough facts, either as to cost or as to quality, to bargain, on an equality with the retailer. He must make his decision to buy or to refuse to buy on the basis of relative marginal utility. The price is asked, and the consumer either decides the article is not "worth" it or another article will do. In other words, the buyer and seller do not build a price anew, from the ground up, by any sort of higgling. Business is a going concern and to-day's price is yesterday's price modified only by some bit of market news. To-morrow's price will be to-day's unless changed by some kind of market news. The center and core of modern business transactions is market news, operating through price changes.

Price setting is a process of adjustment, called bargaining. The basis of bargaining is market news. It is this that keeps the prices balanced to market conditions, whether local, national or international. Some foodstuffs have a world market; their prices are adjusted to world conditions. Everybody knows that the world must eat; the demand is ever present, insatiable. Any substantial decrease in supply brings, as from the dead, the specter of want. It is desirable that foodstuff markets be stabilized as much as possible. The only way to stabilize markets is to stabilize price, and the only way to stabilize price is to make known instantly all the essential facts about supply and demand.

There is the classic story of the elder Rothschild who laid the foundation of the great fortune of that prosperous family. He is said to have been an eye-witness of the battle of Waterloo. Previously, he had arranged for a relay of horses to carry him with the quickest possible dispatch from his post of observation to the Channel and from the Channel to London. He watched the ebb and flow of the tide of battle until the decisive moment came, until the final outcome became manifest. Then he started for London, riding night and day until he reached his destination. For what purpose? To buy stocks on the Exchange. He carried momentous market news. While that news was his alone, he had a monopoly, and on this brief monopoly he laid the foundation of a vast fortune.

The world is not different to-day in its essential business organization. It still pivots on price and the essence of price is still market news. Consider the economic significance of the telegraph, the telephone, the wireless, the newspaper, the postal system, the airplane. Much has been written of these things to show their marvelous ingenuity and convenience. They have broadened the horizon and have brought the ends of the earth nearer together. But greater than all of these things for the welfare of the world is the fact that they carry news of such dynamic force in business. Local markets through them have broadened into national and international markets; local prices through them have become national and international prices.

For the market of any commodity is bounded by an effective demand for it at a prevailing price, and a price will tend to prevail throughout the region where men buy and sell upon the same knowledge of business facts. Wheat is said to have a world market because there is a world price, and there is a world price because it is adjusted to world conditions. Dealing in wheat is a world-wide, going concern; its price is not established anew from the foundation up every day or every minute in the day. Price determination of this, and of every other commodity on the market, is a progressive affair. The old price is utilized in making the new. The price of to-day is not a brand new, hand-made or machine-made, price. It is the interpretation into terms of money of the world condition; it is the best expert opinion of market news.

It may be seen, therefore, that market news is the central organizing force in the market, because it is the essence of market price. It functions as an organizing force through all middlemen, through warehouses, organized exchanges, the wholesale and the retail system.

The justification of such middlemen as jobbers, brokers, commission men, as has been said, is their superior knowledge of the market. In the process of making their organizations effective they tend to disseminate knowledge to producers and consumers; gradually the producer and the consumer draw nearer together and exchange such information as is to their mutual advantage. The middleman whose function is thus absorbed tends to disappear.

Markets are organized for two purposes. One is the actual handling of the commodities, the real process of distributing goods; the other is buying and selling. For intelligent buying and selling market news is essential. It serves more and more this vitalizing, directive function.

**148. Organizations for Securing Market Information.**—For performing this necessary function many kinds of organizations have developed. On the basis of control these organizations are of two different types: (1) governmental, and (2) private.

**149.** *Governmental Organizations.*—There are many Government bureaus for securing and circulating market information. The oldest and best known of the bureaus is the Bureau of Crop Estimates, originally called the Bureau of Statistics, in the Department of Agriculture. On February 25, 1863, the first appropriation of $90,000 was made for a Department of Agriculture. Two years later, 1865, the first distinct provision, $20,000, was made for a statistical bureau. By 1911 the appropriation had reached $225,000.

The Bureau of Crop Estimates gathers statistics on the four great staple crops—corn, cotton, wheat and oats—and issues monthly reports. These reports cover the following three points: (a) the area in acres planted or sown, (b) condition of crops, examination being made monthly during growing season, and (c) the yield per acre at harvest time. Beginning the first of each month a gathering volume of reports will flow from 150,000 or more men conversant with conditions throughout the productive areas, toward the office of the Chief of the Bureau of Crop Estimates. They will carry the conditions as of the first of the month. The facts will be tabulated, State by State, section by section. Then as the eighth of the month draws near, the doors of the rooms where the material is kept are locked; doorkeepers are stationed outside; even the telephone is disconnected. The statistical experts are marooned as if they had the plague.

The reports on these crops are usually "loosed" at two-thirty in the afternoon. As this time approaches, in the corridors are gathered fifteen or twenty newspaper reporters. With them are the operators of the telegraph system, whose instruments stand ready at hand. One minute before the hour set, the doors are unlocked and out step the Chief of the Bureau of Crop Estimates and the Secretary of Agriculture. The Chief holds in his hand 25 typewritten copies of the completed report. Some of these are spread on a table, printed side down. Folded copies are handed to the telegraph operators, and they are not unfolded. Each newspaper man is then permitted to place his hand on a copy, ready to grab and run. As the hands of the clock reach the appointed hour, the Chief of the Bureau shouts "Go!" Within less than five seconds every reporter has disappeared; every available telephone is in use, and the telegraph wires are humming the message of that report. Within fifteen or twenty seconds it is being read in Chicago, New York, New Orleans, and thence spreads with the speed of skillful fingers tapping telegraph instruments, public and private, over the continent and across the seas.

Why all this careful guarding? What is the dynamic power in this simple report? The answer is: Market News! This report carries the summation from 150,000 different sources of facts about crop conditions, of corn, cotton, wheat, and oats, the four great speculative crops. The world price is made of such stuff. It helps to keep that price balanced to world conditions; it aids in holding that price down to a minimum, because buyer and seller both know the facts, because the whole world may know them, because it becomes world news and rumor is killed.

This is only a part of what the Government does for the collection and dissemination of market news. The Bureau of Markets, "to give producers, dealers, and consumers more complete and accurate information regarding current production, market receipts, accumulations both in and out of storage and market demands," has developed a market news service respecting such commodities as grain, hay, seeds, eggs, poultry, cheese, onions, cabbage, and lettuce, as well as meats and meat animals. "These reports tend very materially to steady market conditions by giving the producers dependable information on which to base their business operations."

The Bureau of Foreign and Domestic Commerce collects facts about foreign markets and gives them out to interested parties. The U. S. Geological Survey gathers data on the production and on the deposits of minerals and ores. The Department of Forestry secures data on timber and lumber supplies. In one form or another the Government reaches out into most lines of interest and serves as a medium of market news. Of no small importance is the Daily Weather Report.

For the great fundamental crops there is an international organization. It was instigated by an American economist, David Lubin, and finally organized in 1909. It is called the International Agricultural Institute, and has its seat in Rome. The work of this Institute is carried on by money appropriated by the leading nations of the world, and the information on the fundamental crops is sent broadcast monthly. This is not only one of the great world-price stabilizers, but is likewise a great bulwark against want and famine. It aids in distributing these essential commodities as they are needed, territorially and chronologically.

The Government can act only in the interest of all the people. The market news which it collects must be freely given to all at the same time. On the basis of such common information, competition resolves itself into a matter of careful judgment. It takes away the monopoly of knowledge by the middlemen; it places in the hands of producers and consumers a weapon of defense and of offense. It is well to do so.

Internationally, the nations are becoming more closely knit commercially. The International Institute has, therefore, a distinct service to perform. The Institute thus describes its function:

> The establishing of this Institute is one of the examples of the cosmopolitan nature of modern industry. It is a finger post pointing to the day when the world will be one's home and not the circumscribed boundaries of neighborhood, state, or continent. Every one on the face of the globe is in competition

with every other one, and yet the products of every one are at the command of every one—at a price. Commerce is international; markets are international; economics must be studied as world-wide in its application. The products of every clime find consumers in the utmost parts of the earth, and those who extend their knowledge to world production and world consumption are the only ones competent to handle the marketing problems of the Twentieth Century.

150. *Private Organizations.*—Private organizations for securing business data permeate the industrial and commercial world. The most highly organized of these is probably that of the grain brokers. In such trade centers as Chicago, these brokers have the headquarters of organizations reaching throughout the grain-growing regions. There are experts who make telegraphic reports from time to time on crop conditions, and especially during the critical seasons. The appearance of Hessian fly, or rust, or other pest is quickly noted and discounted in the speculative market price.

The largest private news agency in the grain trade is probably Broomhall's. It has official representatives in all of the great exchanges. "Advices" are received from agents, daily and weekly, by mail, wire and cable. There are more than 300 expert agents scattered through the grain producing countries. Liverpool is the clearing house for it. News can be sent by it from New York to Liverpool and be posted in six minutes. Among private organizations this agency corresponds to the International Agricultural Institute in governmental organizations. A similar organization for cotton is found in the International Cotton Conventions.

Stock brokers also have news gathering and news distributing organizations. This service is largely their stock in trade. When it is recalled that these stock brokers are dealers in contracts, the reason is plain. They need to know more about the market, about demand and supply, than their clients.

Every commodity of sufficient importance industrially and commercially will develop its own trade-information agencies. There is in the United States the Iron and Steel Institute. Abroad, in England, France, Germany, there is a similar organization. The oil interests keep many experts busy with their investigations with a clearing house in the Petroleum Institute.

Market news is often an incidental service performed by organizations formed primarily for other purposes. This is true of the trade associations that have multiplied so rapidly in recent years. There are now literally thousands of such associations, each with its central headquarters from which emanates trade information. Many secretaries of these organizations send out news letters, call conventions, make investigations, and otherwise try to keep their members in the vanguard of progress. The trade journals issued by these organizations contain much trade news. Some of them are published solely for that purpose.

There are many research departments, both in the trade associations and in the larger businesses, whose prime motive is to furnish pertinent trade facts. They are agencies of market news. Banks have organized research departments also, and for the same purpose. Special research companies have recently sprung up to serve as sources of market news.

Special market-news magazines and papers are published. The *New Orleans Cotton Exchange Reporter, Dun's Review, Bradstreet's Review, Broomhall's Corn-Trade News,* commercial and financial and industrial magazines all carry market news, as fresh and up-to-date as possible. The daily papers have their market news sections.

Thousands upon thousands of letters are daily carried by the mail, crammed with market news. The correspondence of the world is doubtlessly very largely made up of trade information. Just as advertising—which, by the way, is a form of market news service—keeps the newspapers and magazines going financially, so trade-information correspondence saves a deficit in the Post Office Department. It is not competition, but market news, that is the life of trade.

The economics of the telegraph system has not yet been written. Nor has that of the telephone system or the wireless been written. Much has been said about the laying of ocean cables, but the romance has been emphasized more than the economic significance. Cables, telegraph wires, telephones, and wireless outfits bring market news from the ends of the earth. In the world markets, the nation that controls the cable systems has the means of controlling the markets. British supremacy in foreign trade was founded not alone upon a merchant marine and foreign investments, but also upon her world-encircling cables. Adequate overseas communication is as important as ships and foreign banks to successful foreign trade.

Cables, like ships, are, in times of peace, supposedly employed freely in the service of the world; in time of war they are at the disposal of the government where ownership lies. For years the British cable-rate blanks have carried the following provisions: "The dispatches of the imperial (British) government shall have priority when demanded. The cable must not, at any station, employ foreigners; and the lines must not pass through any office, or be subject to the control of any foreign government." It is significant in this connection to note that only a single line, that of the Compagnie Française Cables Télégraphiques, which does not touch foreign land, runs between the United States and Europe. The question has been raised and will rise again as to whether or not it is possible to neutralize all international cable lines.

Steamboats carried news faster than the old sailing vessels. The cable easily outdistances the steamer. But the cable lines are relatively expensive and afford only a restricted means of communication. Only recently another possible means of transoceanic communication has been opened up. An airplane successfully crossed the Atlantic in a single flight. An airship has made a successful round trip. There is already much speculation as to the possibility of this medium in supplanting to a very considerable extent the cable in carrying messages over seas. This initial passage of the airplane was made in sixteen hours from Newfoundland to Ireland. The crossing is so much more rapid than the steamship that it is supposed a great part of commercial communication can be done in this way.

Essential market news is served luxuriously in hotel, club, or office by means of that marvelous little instrument called the "ticker." Hitherto, these tickers have been the quickest method of transmitting news widely. A private telegraph or telephone wire gives equal speed, as well as privacy, but a single master transmitter can send the important news out to many of these little tickers instantaneously. "The service gives out news to the 'Street' where it is most needed, for without an up-to-the-minute knowledge of what the outside world is doing, rumor is much more likely to affect the sensitive market. The newspapers with their hourly editions do not come often enough. The news must come hotter and faster than these possibly can."[1]

Through all of these means, private and governmental, trade information is collected and distributed. Gradually, faster and faster methods have been developed, until now the news flies almost with the speed of light. This market news system has become the very core of the market organization, in every respect as essential as the railroad or the warehouse.

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[1] *Technical World,* vol. xxi, p. 264.

**151. Essentials of Market News.**—There are two general phases of trade information; one has to do with production, the other with the demand. In those essential products with a world-wide and relatively inelastic demand, the attention turns toward production. Thus, crop reports sent out by the Government deal with (1) acreage planted, (2) condition of crops during growing season, (3) yield per acre, (4) total production, (5) average prices per bushel, (6) total farm value, (7) stocks on hand at given times, (8) amount shipped out of country of production, (9) concise statements of weather conditions throughout the productive area, and (10) the "visible supply."

As has been pointed out before, it is important to trace the relation between the volume of production, the total value, and the visible supply. This last term signifies, in general, the amount within sight of the market; that is, the amount in elevators, on board cars, loaded on ships, etc.—the amount that has been charted. The visible supply becomes increasingly important as the end of the crop season draws near. The amount of wheat left at the end of May, the bales of cotton remaining after August 31, the number of bushels of corn left after September, show the real surplus of the previous crop to compete with the new crop.

For other commodities, other points may rise in importance. The driving of new oil wells, the opening of new mines, the total production of ore, coal, lumber, the recent estimates by experts of remaining supplies, are all pertinent.

But production figures are significant only in relation to demand. This may mean the demand for finished products reflected back to raw materials. It certainly includes the results of a careful analysis of the market. The chief elements of this analysis have already been discussed. The principle to keep in mind is that any pertinent fact, touching either the production of a commodity or its consumption, is trade information, and may become an influence in affecting market price, and that a market price at any given moment is an understanding of supply in relation to demand on the basis of known trade information.

**152. Control of Trade Information.**—So fundamentally important is trade information in the intelligent direction of industry, so tremendous the advantage in a monopoly of essential trade facts, that the question of control arises. Should the machinery for the collection and distribution of market news be left to private control? The grain brokers have such an efficient organization for securing news that they can keep at least two weeks ahead of Government sources. This means that all of the reports on the great speculative crops that are given out on the eighth of each month by the Department of Agriculture have already been discounted in the market. The producer or buyer who does not have such an organization may therefore feel at a great disadvantage in bargaining.

In this connection it is important to inquire where the market price is really determined; whether in that market center through which the bulk of the commodities passes or in that market center where the market news is concentrated? Specifically, is the world-price of wheat determined in Chicago, Minneapolis, Duluth, or in Liverpool; is the world-price of cotton determined in New Orleans, New York, or Liverpool, or Manchester; is the world-price of copper or steel determined in New York or abroad; is the world-price of wool determined in Boston or London; is the world-price of petroleum determined in the United States or abroad; is the price of coffee determined in Sao

Paulo or in New York? In a sense these queries are academic in character, because a market price may be built up by adding transportation, handling and storage charges, or may be taken apart by deducting them. That is, the Liverpool price may be the Chicago price, plus charges, or the Chicago price may be the Liverpool price, less charges.

There is a point here worth considering. Does physical control over a substantial quantity of a commodity give the advantage over a superior knowledge of the world news? The problem is easily solved. Marketing is a going concern, and price adjustments are made on the basis of news. Where that news is concentrated will be found the dominant price factors. It follows, too, that a combination of physical control and market news is doubly strong. In Bremen, Germany, was the center of the world's copper market, because it was the center of the world's copper news. If the cables of the world are centered in Great Britain, there will be found the dominant world-price factors. Banking, shipping, trade, will follow. Advance news, even if only by a matter of seconds, permits the discounting in terms of price.

It is clear, then, that a real question does exist as to whether or not individuals or governments should have control of the machinery for collecting and distributing market news. The United States endeavors to make the essential crop news common property, so that the humblest producer may read in the paper the same facts as the cleverest broker. The International Agricultural Institute is trying to make this service international. Like all other industries, that of dealing in market news will be declared a public utility when the people realize its true significance.

**153. Discounting the Future.**—Buying and selling future contracts is like crossing a bridge before one gets to it. There is a calculation of what will happen; it is a case where coming events cast their shadows before them. Future dealings are really the shock absorbers in business. In our modern roundabout business, speculation, that is, buying and selling future contracts, is absolutely necessary. When this speculation is rendered as intelligent as possible through a study of trade information, the fluctuations in market prices are leveled out and the risks of business are minimized. This is a most important service. It has often been observed that the actual transpiration of an event does not have the effects upon the sensitive exchanges that might have been expected from its significance. This is due to the fact that its effects have been anticipated and discounted. The anticipation of effects is discounting the future. The stabilizing results, beneficial to producer, to middleman, to consumer, in the reduced risks of business, are due to market news.

**154. Trade Information and Competition.**—Competition in trade may be based upon the effort to secure better trade information or upon the effort to judge most accurately the effects of market news. The former kind is inevitable under private individualistic competition, where private enterprise is superior to public enterprise in securing the essential business facts. In some cases the government can maintain an organization of a magnitude that is impracticable for private enterprise. The German government had a system for securing information from all parts of the world, through foreign trade agents, foreign branch banks, government agents, missionaries, emigrants, steamship companies, beyond anything an individual firm could do. No British business firm could match the resources of the British Board of Trade. No American firm has the potential power of our consular and trade-commissioner service.

The danger of leaving market news to private control lies in the abuse of its power. In the market it is literally true that knowledge is power. During the month of July, 1916, favorable reports were pouring into the Chicago Board of Trade as to the condition of the spring wheat crop in the Northwest. One day a certain brokerage firm got a telegram from an expert at a small town in Nebraska. Immediately, a member of the firm boarded a train for that place. Upon his arrival, he hired a powerful motor car and started to drive northward through the spring wheat region. With practised eye he examined field after field for signs of rust, of which the telegram had spoken. After a trip of ninety miles or more he stopped, for the signs had ceased. But this expert had discovered enough; he knew that the fatal rust was rapidly spreading north through the entire region, and that if the hot moist weather, with a prevailing south wind, persisted a large part of that important crop was doomed. He telegraphed this news to his firm.

With this information that brokerage firm in a few minutes could capitalize its position to the limit. It was a monopoly for a brief space of time, as complete as monopoly can be. Its power was as great as that of a "corner" in the market, while it lasted. Is this only a part of legitimate competition? There is no question of false information, of "tips" from unreliable sources. This is not a "bucket shop" method. But it is still an open question as to whether or not private competition should extend this far.

**155. Use and Abuse of Trade Information.**—There is, of course, a right use and a wrong use of market news. In all cases the news should be reliably true. Falsification, by exaggeration or by depreciation, can never be right. Organized exchanges have very strict rules in this regard, because they have learned by the bitter experience of public disapproval that honesty is the best policy. It is not defensible, either, to issue reports as fresh that have already been discounted in the market. The news coming through the "ticker" service is condemned by the experts on the exchanges as "gossip," because the facts have already passed through the hands of those who have had every reason to use them for their own advantage.

It is easy to start a rumor in an uncertain market, and unfounded reports have a remarkable tendency to grow fast. Any "manipulation" of this sort is to be utterly condemned. Nothing can insure the right use of market news besides an unswerving honesty and integrity. The individual may be able to escape with the plunder derived from false reports, but the institution through which he works will sooner or later have to bear the responsibility. Stock markets testify to this fact, as do also commission merchants. The evil practice of one man may undo the good work of a score of other men. This statement is peculiarly true in the use of market news.

**156. Market News as a Business Force.**—It must be realized clearly that market news is not in itself either a function or an institution; it is an active force, an active business force, subtle, intangible, pervasive. It is a motive power of judgment. "Carriers may be provided to transport the crops to market; local, central, and retail markets, elevators and warehouses, exchanges and other market places to facilitate their storage, preparation and sale; but without authentic current trade information the machinery of distribution could not but operate in a haphazard manner, and prices would seldom, if ever, be such as the actual or probable supply and demand naturally warrant."[2]

Market news, while not a function in itself, performs a most essential commercial function. It is an organizing, directive force; it is an intelligent use of business facts for the purpose of business management. Under a régime of individual enterprises, men do what pays best, or what they think pays best. The determination of what pays best is based on the individual's interpretation of trade information as he knows it. This applies both to industry and to trade. More and more, commodities are being diverted *en route,* on telegraphic advice as to market conditions in certain trade centers; more and more, producers whether farmers, manufacturers, or mine operators are directing their operations by market news. Through the medium of market news the economic process from beginning to end becomes more intelligent.

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[2] Huebner, *Agricultural Commerce,* p. 293.

An increasing factor in market news is the knowledge gained from scientific research. "The chemical laboratory is now a necessary part of every steel plant, fertilizer factory, and dye works. Manufacturers in every field, seeking to better the quality of their products or to reduce costs, have found the services of the chemical engineer indispensable. Old rule-of-thumb methods have been scrutinized in the light afforded by scientific experimentation, and great improvements have been made in fundamental processes, especially in the utilization of by-products that had been considered waste and discarded."[3]

Market news is, therefore, not only an organizing and directive force, but also a conserving force.

## SUGGESTIONS FOR STUDY

The student should now investigate the machinery that has been developed for collecting and circulating trade information on his chosen commodity. For class room discussion the following topics will serve:

1. Market news as a directing force in business.
2. Development of market news agencies.
3. Business barometers.

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[3] Smith, *Strategy of Minerals,* p. 212.

4. Prophesying the future of business conditions.
5. Scientific analysis of business facts.
6. Translating business facts into prices.
7. Market news for producers.
8. Market news in the bargaining process.
9. Trade information and the middleman.
10. Trade information as a specialized function.

READINGS:

U. S. Bureau of Crop Estimates, Farmer's Bulletin No. 581.
Monthly Crop Report.
Circular 17, Government Crop Reports.
U. S. Census Office, Bulletin 125.
Monthly, bi-monthly, annual reports.
U. S. Weather Bureau, Monthly Weather Review.
Bureau of Foreign and Domestic Commerce, Commerce Reports.
International Agricultural Institute, *Monthly Report.*
*Broomhall's Corn-Trade News.*
*Dunn's Review.*
*Bradstreet's Review.*
"Current Sources of Information in Produce Markets," *Annals of the American Academy of Political and Social Science,* September, 1911.
"The Crop Reporting System," *Annals of the American Academy of Political and Social Science,* September, 1911.
*Babson's Desk Sheet of Tables on Barometric Figures and Business Conditions.*
Duncan, *Commercial Research,* Chaps. IV, IX.
*Journal of Commerce,* New York.
*Commercial and Financial Chronicle.*
Daily papers.
Massachusetts State Board of Agriculture, Circular No. 76, "The Value of Market News Service to Farmers and Fruit Growers."

# CHAPTER XI

## MARKET PRICE

The forces of supply and demand meet in the market and culminate in a market price. The value of a commodity is there expressed in terms of the medium of exchange, that is, in terms of money; legal title passes from one individual to another, and along with it the risks and responsibilities. Commodities may be sold many times before they reach the consumer. At the other extreme are the raw materials that enter into a finished product without being quoted in the market. In every case, charges are running constantly against commodities while they remain in the economic process. There is, therefore, a series of price steps or margins.

Market prices may take their names from the market in which they are quoted or from the dealers who quote them. In the former case, there are local prices and wholesale market prices. In the latter case, there are producers' prices, farm prices, wholesalers' prices, retailers' prices, consumers' prices. If these latter prices are followed through step by step, the final composite price can be more clearly understood. It is proposed here to discuss the subject from this point of view.

**157. Price Factors and Influences.**—A comprehensive view may first be taken of the complex of factors and influences which enter into market prices. It is not possible to name them all, because they not only differ at different times, but some of them are too subtle and intangible to be isolated and defined. The following statement may be taken as a fairly comprehensive one:

> No attempt has been made to investigate the causes of the rise and fall of prices. The aim has been to give only the prices as they actually prevailed in the market and such summaries thereof as appear necessary. The causes are too complex, the relative influence of each too uncertain, in some cases involving too many economic questions, to permit their discussion in the present report. An enumeration of some of the influences that cause changes in prices may be of interest, however. Such influences include variations in harvest, which not only contract or expand the supply and consequently tend to increase or decrease the price of a commodity, but also decrease or increase, to a greater or less degree, the purchasing power of such communities as are dependent in whole or in part upon such commodity; changes in demand due to changes in fashions, seasons, etc.; legislation changing internal-revenue taxes, import duties, or bounties; inspection as to purity or adulteration; use of other articles as substitutes—as, for instance, an advance in the price of beef will cause an increased consumption of pork and mutton and, it may be added, a probable increase in the price of both pork and mutton; improvements in methods of production which will tend to give either a better article for the same price or an equal article for a lower price; cheapening of transportation or handling; speculative manipulation of the supply or of the raw product; commercial panic or depression; expanding or contracting credit; overproduction; unusual demand owing to disputes between labor and capital in industries of limited producing capacity, as in the anthracite coal industry; organization or combination of mills or producers, thus enabling, on the one hand, a greater or less control of prices or, on the other hand, economies in production or in transportation charges through the ability to supply the article from the point of production or manufacture nearest the purchaser. No conclusion can be formed safely as to causes without an examination of the possible influence of several—in some cases perhaps all—of these causes. For example, the various internal-revenue and tariff

acts have, in a marked degree, no doubt, affected the prices of proof spirits, of tobacco, and of sugar; but, on the other hand, they have not been alone in their influences, and it probably would not in all cases be accurate to give the change of tax or duty as representing the measure of a certain and definite influence on the prices of those commodities.[1]

The theorist goes far beyond these factors and influences. "Back of these causes lie other causes, multiplying endlessly as we proceed backward. But if we trace back all of these causes to their utmost limits, they will all resolve themselves into changes in the marginal desirability or undesirability of satisfactions and of efforts, respectively, at different points of time, and in the marginal rate of impatience as between any one year and the next."[2]

The following causes have also been enumerated in the order of their importance in affecting commodity prices: "(1) Increase of gold supply, (2) exhaustion of natural resources, (3) rising standard of living, (4) withdrawal of population from agriculture, and growth of cities, (5) trusts and combinations, (6) tariffs, (7) labor unions, (8) growth of population and unscientific methods of farming, (9) extravagance in expenditure, (10) waste and fraud in distribution, (11) uneconomical marketing and housekeeping, (12) speculation, (13) immigration."[3]

But it is not to be understood that these or any other set of factors and influences enter consciously into the construction of every price, or indeed of any price. The practical fact to be remembered is that business is a going concern, that price making is a progressive affair, that no price in the market to-day is built from the foundation up, that to-day's price is yesterday's price modified only by some bit of market news. In the long-time period, every factor and influence will have full effect, but from day to day there is only a step at a time.

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[1] U. S. Bureau of Labor Statistics, Bulletin No. 114, p. 22.

[2] Fisher, *Elementary Principles of Economics*, p. 409.

[3] Babson, *The Annals of the American Academy of Political and Social Science*, September, 1911, p. 174.

All economic forces are finally concentrated in market price. Here is found the composite opinion of the best business minds, which have transmuted market news into the dollars and cents of price. This is the higgling of the market; it is the meeting of the minds of buyer and seller; it is the economic consummation so devoutly to be wished.

**158. Local Market Price.**—The first price set upon commodities in the local market may be called the local-market price, or farm price or the price at the source. It is clear that the minimum at which this price can run for a long period is the cost of production. Farm experts have claimed for several years that farmers have been selling the fertility of their soil; it has often been estimated that the local price received for petroleum and for gold and silver has been less in total sum than the amount of money spent in drilling, mining, and prospecting. Generally speaking, however, the local-market price must at least cover the cost of production, in so far as this is known.

In the case of such a commodity as grain or cotton, however, the cost of production is so difficult to determine and varies so greatly from season to season and from section to section that the growers' cost of production does not directly determine the local prices. Rather the dealers will usually deduct from the primary-market price the freight charges, plus an added number of cents per bushel or bale to cover all expenses for handling and including a commission or profit. Thus, Kansas wheat that was quoted in Kansas City at 97 cents per bushel, "spot" price, brought in the local market 87¾ cents. The freight was 5 cents, the elevator charge 3 cents, and commission and other charges 1¼ cents. In another case, on September 28, 1914, "an elevator which allows a margin of

3 cents per bushel on all wheat purchased, received several track bids averaging 90¼ cents per bushel, basis No. 2 hard, which is the contract grade in Kansas. The quotation to farmers on this day was the 'on track' price quoted the elevator, less its margin of 3 cents, or in this case making the price to the farmer 86¾ cents per bushel."[4]

The average cost to haul grain to local market, as estimated by the Department of Agriculture in 1906, was 9 cents per 100 pounds. "The average cost for hauling all farm produce to market is about eleven cents per hundredweight."[5]

In a similar way the local price of cotton may be determined by the Liverpool price. If the Liverpool price is, say, six pence, or 12 cents, charges may be deducted for tare, inland freight, compressing, ocean freight, insurance, expenses of doing business, profit, totaling about 2 1/10 cents. By subtracting this latter sum from 12 cents the farmer's price will be 9 9/10 cents.

A special commission was appointed by the U. S. Food Administration, in the Chicago market, to determine the proper price to be paid to milk producers so as to cover the cost of production plus a fair profit. The items of cost considered by the commission were as follows: grain, silage, hay, bedding and roughage, and labor per 100 pounds of milk. A profit of ten per cent was added to the cost. This was an instance of calculating logically the local market price from the ground up.

What may be termed the local price of coal includes resource cost, or what is charged against the marketed product as the value of the coal in the ground, and the mining cost or charges for wages, supplies, power, overhead and selling costs paid by the coal operators. "This cost plus the resource cost—the royalty or depletion charge—and the profit or loss on the sale make up the value at the mine mouth.'' It was estimated by experts that the mining cost of bituminous coal was one dollar per ton and of anthracite $1.86 in 1909. The resource cost on anthracite has been calculated to be about 32 or 35 cents per ton, on bituminous about five cents per ton.

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[4] House Document 1271, 63d Congress, 3d Session, p. 5.

[5] Adams, *Marketing Perishable Farm Products*, p. 58.

From this brief survey of local prices several important points may be illustrated. In the first place, commodities with a world market are acted upon by world forces and local prices are often determined by deductions from the central-market price. This is an instance where the superiority of market news is revealed. Generally, the local producer has little or no conception of the bewilderingly intricate cross-currents of forces that make up the world price. Or again, as the value of cost accounting is understood better the local price may tend to be adjusted to the cost of production plus a sufficient profit to secure adequate output. The lack of accurate information in general on the part of producers renders them more or less helpless in bargaining; the price is usually determined for them and not by them. The need for more complete analysis of costs is patent here.

**159. Primary and Terminal Market Price.**—As goods pass from the local market to the primary and terminal market, they enter the wholesale market system. Here there is a high type of organization; trained mind meets trained mind; knowledge is pitted against knowledge. The great forces of demand and supply work here under the most intelligent direction. The wholesale prices are the standard in accordance with which practically all other prices, especially of agricultural commodities, are gauged. ''Wholesale prices are more susceptible to, and they more accurately conform to, the various elements affecting demand and supply than do either retail or farm prices.''

It is practically impossible to ferret out all of the influences that are at work upon the wholesale market prices. There is no single price; for prices are composites; they are the result of complex action. To escape a bewildering maze, it is necessary to keep in mind the fact that the price of to-day is really an inheritance of past years, that prices tend to persist unless there is tangible reason for change, that the true difficulty is to transmute an item of news into terms of price. Some change in the field of production or in the field of consumption will spread by direct or by indirect influence through the entire system, becoming less and less as it spreads. For the wholesale market price is a system with no logical beginning or end.

The aim of any one seeking to understand the wholesale price of any given commodity should be to isolate the controlling factors. The purchasing department of a large cereal manufacturing concern, in order to master the wholesale-price factors in the primary market for grain, plotted those prices from 1869 onward, accounting as fully as possible for every fluctuation. With this analysis it became possible to work more intelligently toward foreseeing the trend of prices, for the price of the day has a relation to past prices and to future prices.

The future price is a speculative price in the sense that many influences are uncertain, but even in such a price it is possible to ascertain constant factors. Some kind of a charge is always running against commodities until they are consumed. The December quotation for May wheat will differ from the "spot" price by at least enough to cover storage and insurance. In the case of a perishable commodity, such as eggs or apples, there will be added to the storage and insurance an item for deterioration. The calculable charges against a shipment of cotton will include the following: freight from interior point, compressing, ocean freight, fire and marine insurance, wharf-age and dock dues, storage, weighing, sampling, inspection, brokerage and commissions, exchange supervision, weight franchise, foreign-exchange brokerage, patching, repairing, bagging, interest, expenses for wages, cables, telegraph. With all of these charges, the whole cost to Liverpool, before the World War, was not over one cent per pound.

It is clear that the performance of every function in the marketing process is a charge against each commodity. The more difficult and hazardous the function the higher the charge. Time and place values are greater for perishables than for coal or pig iron. Take an example of citrus fruit. The cost per dozen of marketing California oranges in eastern markets based on an assumed retail price of 40 cents per dozen shows that the grower receives 10.7 cents, picking and hauling to packing house cost 1 cent, the packing house cost is 2.9 cents, freight and refrigeration cost 8.2 cents, the grower's selling cost is 0.6 cent, and the jobber's margin is 3.3 cents.[6]

The wholesale market is the scene of the adjustment between demand and supply. The big packers of meat in Chicago stand in a strategic position between the producers and the wholesale market. It is only natural that the price offered by them for livestock coming into the stock yards should be affected by their telegraphic reports from their branch distributing houses. In general, the livestock sellers know neither side of the story thoroughly. They feel, therefore, at a disadvantage in bargaining. The packers, too, by long experience know to a nicety the effect upon the flow of livestock to market of each price change. In so far as possible the price they offer brings in the quality and quantity for their weekly "packs."

A tabulation of livestock prices in comparison with the wholesale prices of meat for 1914 and 1915 showed for cattle and beef the following facts: (1) The wholesale meat price is far more sensitive than the livestock price in the stockyards, to changing conditions. (2) The price sometimes rises in the face of increasing supply. (3) Prices sometimes fall when the receipts show no general increase and even when the receipts are on the decrease. (4) Prices sometimes remain practically constant through a period of increasing or of decreasing receipts. (5) Prices in the wholesale meat market are more sensitive to changes in the market for meat, and move more nearly in sympathy with these changes, than they respond to changes in receipts. (6) The price line does not show distinct seasonal changes.

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[6] Powell, *Western Fruit Jobber,* April, 1915.

This examination shows that supply and demand in this complex industry do not have a simple and direct effect upon price. There are many factors to be considered. In the wholesale milk price there is a clearcut distinction between seasons. Usually there are two price contracts per year: one for summer milk and the other for winter milk. Even these may be graduated by the month to represent changes in cost of production. A highly seasonal perishable commodity will show a more decided fluctuation. That the prices of such perishables have been leveled out by means of the cold storage warehouse is shown by the following graphs drawn by the Bureau of Statistics of the Department of Agriculture.

The conclusion from the above study is also of great significance in relation to prices in the primary market. "The principal point of interest in this comparison is to discover how closely, or otherwise, prices at the farm vary from the other prices. The general fact appears that farm prices vary with city prices, sometimes closely, and often roughly so. Sometimes it is the farm price that follows the city price, and sometimes it is the city price that follows the farm price, if one may depend on these tables for the inference."[7]

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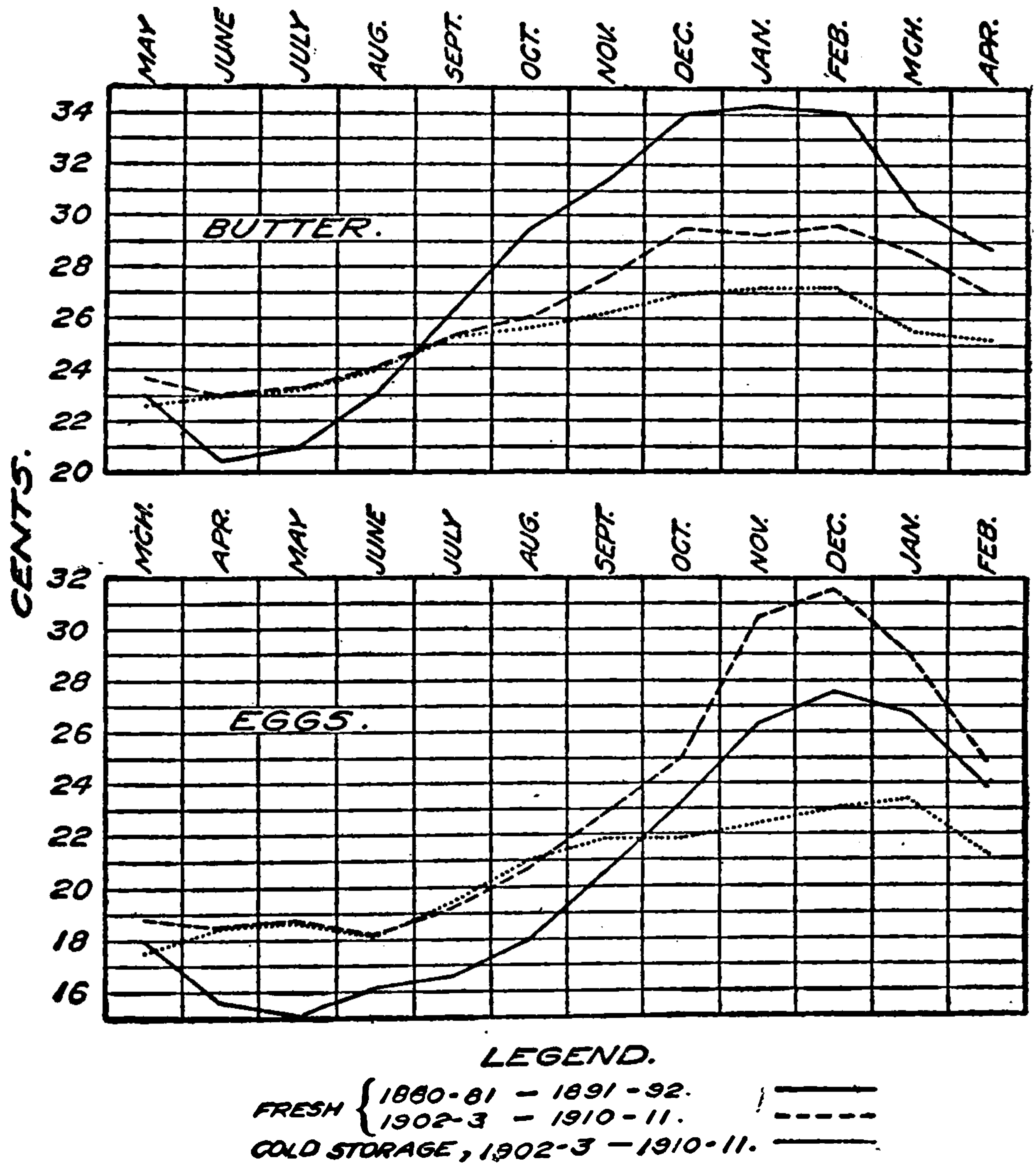
[7] *Ibid*, p. 70.

The prices in wholesale markets tend more strongly to be leveled out to an adjustment between markets representing costs of transporting, than local prices. In a highly



CHARTS SHOWING EFFECT OF COLD STORAGE ON BUTTER AND EGG PRICES

organized business, as that of wheat, markets are kept closely adjusted through arbitrage. In perishable products the diversion of cars in transit aids greatly in price adjustment. In spite of all efforts, however, prices do get out of joint. But prices may readily get out of joint, for prices constitute a system in the literal sense that they are so connected as to make a complex whole. To understand the workings of this system at any given time and the changes it undergoes from one time to another, it is necessary to trace the interconnections among different parts of the system. These interconnections are numerous and varied in their character. The whole system of prices is not a miscellaneous aggregate of simple commodities, but an organized combination of groups of commodities. The prices of articles within this group have especially intimate relations with each other and the groups themselves cross each other in rather perplexing ways.[8]

**160. Retail Prices.**—Since raw materials run largely on the basis of wholesale lots, the problem of retail prices is not so fundamental. Foodstuffs, however, pass on to the consumer for the most part without manufacture. It is here that the problem of retail prices arises. Something needs to be said, therefore, about the retail price system.

Goods flow into the wholesale market in large lots, are there graded, broken up and sold to the retailer in smaller lots. The retailer in turn sells in smaller lots still to the consumer. In general the margin between the producer's price and the wholesale price is wider than that between the wholesale price and the retail price. This means that on the whole the public is a better buyer than the producer is seller.

Another characteristic of the retail price is that it is not so sensitive to change as the wholesale price. The reason for this is largely psychological. It is to be remembered that the retailer meets the consumer face to face, and every change in price, especially an increase, may need explanation. A maker of macaroni debated for some time the best means of getting the retail price of his goods increased. They were sold in a package at a uniform

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[8] Mitchell, *History of Prices During the War*, Summary, p. 92.

### Table Giving the Price Received by the Producer and each Middleman and the Per Cent Increase of each Price over the Preceding Price, together with the Total Increase of Consumers' Prices over Producers' Prices[9]

| | FARMER | PLUS FREIGHT TO TERMINAL | | JOBBER | | WHOLESALER | | RETAILER | | Per Cent Increase of Consumer's Prices over Producer's Prices |
|---|---|---|---|---|---|---|---|---|---|---|
| | Price Received by | Amount | Per Cent increase over preceding Price | Price Received By | Per Cent increase over preceding Price | Price Received by | Per Cent increase over preceding Price | Price Received by | Per Cent increased over preceding Price | |
| Butter (low grade) per lb........ | $.18½ | $.19 | 2 | $.21½ | 13 | .24 | 11 | $.32– .38 | 33– 58 | 73–105 |
| Butter (high grade) per lb........ | .23 | .23½ | 2 | .26 | 10 | .29 | 11 | .40– .45 | 38– 55 | 74– 96 |
| Potatoes (low grade) per bushel*. | .53 | .62 | 17 | .68 | 9 | .75 | 10 | 1.10– 1.30 | 46– 73 | 108–145 |
| Potatoes (high grade) per bushel.. | .63 | .72 | 14 | .80 | 11 | .90 | 12 | 1.30– 1.60 | 44– 78 | 106–154 |
| Eggs (low grade)† per doz........ | .11 | .12 | 9 | .13½ | 12 | .15 | 11 | .25– .30 | 67–100 | 121–173 |
| Eggs (high grade) per doz........ | .21 | .22 | 4 | .24 | 10 | .27 | 11 | .35 | 30 | 67 |
| Huckleberries (low grade) per qt... | .04½ | .05½ | 22 | .06 | 9 | .07 | 16 | .12 | 71 | 166 |
| Huckleberries (high grade) per qt.. | .07 | .08 | 14 | .10 | 25 | .11 | 10 | .15 | 36 | 114 |
| Blackberries (low grade) per qt ... | .04 | .05 | 25 | .05½ | 10 | .06 | 13 | .12 | 100 | 200 |
| Blackberries (high grade) per qt.. | .06 | .07 | 16 | .08 | 14 | .09 | 12 | .15 | 66 | 150 |
| Live Poultry (low grade) per lb... | .06 | .06½ | 7 | .09 | 38 | .11 | 22 | .22 | 100 | 266 |
| Corn per doz.................... | .15 | | | | | | | .40 | | 167 |
| Tomatoes per peck *........... | .32 | .32½ | 1 | .36 | 10 | .40 | 11 | .80 | 100 | 150 |

* This is the total price when sold in the quantities the average purchaser buys; that is, a basket of potatoes and a quarter or half peck of tomatoes.

† In many cases these eggs are candled and sixty per cent of them sold as freshly gathered eggs,—the others being sold as "rots and spots," etc. In other cases, however, they are sold to the consumer as eggs fresh from the farm. Thus one man writes that they sell them as such and asks: "What is the effect of the egg law on us?"

[9] Table from King, "A Study of Trolley Light Freight," *Annals of the American Academy of Political and Social Science*, vol. l, p. 13.

price; they were known in the trade by a package of standard size at a fixed price. The possibilities were to reduce the amount in the package, to increase the size and price of the package, or to raise the price on the original package. It was clearly a question of consumer psychology. But the manufacturer endured for a long period the increasing pressure of costs before any change at all was made.

The retailer is anxious to keep his goods moving; small capital with rapid turnover is good business. His price must, if possible, be such as to move the goods. Deterioration, especially in perishable goods, is rapid, and the risks are correspondingly large. The margin between cost and price is therefore made as wide as can be done and get the goods sold. The retailer's margin on groceries runs from 25 per cent to 40 per cent. The most common figure, that is the mode, for the total expense of a grocery store is 16.5 per cent, with an annual profit concentrating about 4.5 per cent.[10]

Like wholesale prices, the retail prices form a complex system. They are related to all of the prices that have preceded, and they have interrelations of their own. Whatever affects purchasing power affects retail prices. The prices of substitutes and of by-products of great industries are factors in the retail price. Nevertheless, the retail prices are dependent upon the wholesale prices, just as is true of the farm prices of many commodities. In the entire price system, the wholesale price is most highly organized, most sensitive to changes, has more frequent but on the whole less violent fluctuations, and is usually the controlling price for both producer's prices and retailer's prices.

The table on page 236 will illustrate the entire price system, from producer to consumer, for certain perishable commodities in a single city market.

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[10] Bureau of Business Research, Harvard University, Bulletin No. 5, p. 8.

The great disturbance in prices of every kind caused by the World War has appeared with exaggerated effect in the retail-price system. Production was disrupted and output was greatly lessened. The public read on all sides about shortages in supplies; it was educated into expecting abnormally high prices. There was no longer need for the retailer to defend the increase. In fact, the whole price system broke loose from its moorings. Consumers had no means of defence against high charges. Wholesale prices rose to such a height as to carry along with them the entire system to a new level.

> There has been no other revolution in prices so sudden, so violent, and so widespread as the revolution that accompanied the war of 1914-1918. . . . The price problems with which all commercial nations are now concerned spring directly from this shifting of price levels during the war; but these problems look to the future, not to the past. Is the period of violent fluctuations closed, or is a counter-revolution coming? If prices fall, when will the fall begin, what commodities will go down first, and how far will they drop—back to the pre-war level? Or should every one adjust his plans to the expectation that prices will remain indefinitely at their present height? [11]

Certainly, the high retail prices of many commodities will, through the wholesale price, influence production. "Once a rise of prices is started in any important branch of business it tends to spread to other branches and to call out increased production. This development is characteristic of every period of increasing business prosperity after it gets under way. It appeared in very pronounced fashion during the war." [12]

This experience further illustrates that the retail price tends to stabilize at a "level," unless it is thoroughly disturbed by some far-reaching influence. The record for the past seventy-five or eighty years reveals an upward movement stage by stage, with a setback from time to time during a period of depression.

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[11] Mitchell, *op. cit.*, Summary, p. 3.

[12] *Ibid.*, p. 39.

Changes in methods of distribution, reductions in cost of producing and of handling goods, new means to secure economy, the elimination of wastes, whatever affects individual commodities, will inevitably find their way into the retail system. All of the psychology of salesmanship finds place here, too, such as odd prices, price cuts, special sales prices, the advertising of prices, the emphasis upon quality. The art of salesmanship is an important factor in the retail price. There are also monopoly prices and competitive prices. Probably the most important factor in the recent development of retailing is the trade association,—local retail associations, such as the retail grocers association, retail hardware association, association of retail shoe dealers, and so on. Through these associations retail prices tend to be leveled out from section to section. Formerly there might be a considerable difference in price even within the local retail market. Now this is more and more rare. These associations have become a great leveling and stabilizing factor.

**161. Price Quotations.**—Wholesale as well as retail prices are often quoted in the papers. It is important to know what these quotations mean and how they are arrived at. In the exchanges the quoting of prices is carefully regulated. At the opening of the exchange each morning there is a bit of flurry in buying and selling, a playing for advantage between the bulls and bears, for the first sale makes the "opening" price for the day, and fluctuations up or down are calculated from it. There is a corresponding struggling just before the closing gong strikes. Between these two prices all variations are recorded, together with the amount bought or sold at the new price. All of these prices are reported and spread broadcast throughout the country. They represent, however, prices for the basic grades of commodities. In addition, there may also be given in the market reports what is bid or at what figure the commodity is offered.

In the stockyards the day's prices are quoted for different grades of livestock, and the ranges in price are usually given. It may happen that no single transaction has taken place at the figures quoted, but within them the sales have taken place. These price ranges are secured by a special reporter who circulates from day to day among the commission men and stock buyers and makes inquiry. On the Butter and Egg Board the prices, bid and offered, are written on the blackboard, but the reported quotations are secured in much the same way as in the stockyards. In the produce market the representative of the official bulletin interviews, for instance, the "dressers" and live-poultry men regarding prices for the day; and having formed his own judgment of the feeling at the time the session is on, he establishes the quotation for the day. It may be said, in general, that market quotations belong to the newspaper business rather than to the market. The reporters go about the street and find out the views of different merchants, and out of these "talks" develop the price quotations for the day.

These methods of quoting prices are very different from quotations sent out in answer to inquiries. The latter constitute a legal offer; the former do not. General price quotations, such as appear in the newspaper, are far less definite than the quotations sent out, for instance, to country elevators by grain brokers, or to local markets by butter and egg commission men. The livestock man who reads a market quotation in his paper cannot be assured that he can obtain it actually. In fact, market quotations are open to all the abuses of market news, of which they are a part.

It is an open question whether or not they should be left to the control of private business.

**162. Price "Steps" or Intervals.**—When changes in prices occur, they take place on the basis of intervals or steps determined largely by the degree of organization in the market and by business practice. In a highly organized market, like that of grain or cotton, changes in price occur as narrow as a fraction of a cent, say one-eighth. Foreign exchange quotations run as narrowly as one-sixty-fourth of a cent. More fractional changes are made in the wholesale price than in the retail price. In fact, change margins on the whole are much wider in the retail market than elsewhere, and in "fancy" goods, or where price is a minor consideration, than in staples. Prices in a fraction of a cent do not occur in retailing except for more than one unit, because change cannot be made. Quotations are made, therefore, such as the common one of 13 cents each or two for 25 cents.

Wide margins appear not only when changes are made in the price, but also between grades. "Fancy" grades carry a price removed by a wide margin from common grades. Grapefruit may have a common grade at 10 cents apiece, with the next grade 15 cents each. This difference of five cents is not arrived at by careful study; it is merely the next "step." In this matter of price graduation, as in quoting prices, there is opportunity for abuse, especially because the consumer is becoming less and less expert as a bargainer.

**163. Sympathetic Prices.**—The sensitive point in marketing for the great mass of people is the daily price of the things they buy. So subtle and intangible are the forces at work upon the marketplace, so complex and indeterminable the influences registered upon the sensitive dial of market price, that the general consumer despairs of understanding and acquiesces so long as he can endure the stress.

But probably the most baffling phase of the whole price problem is that of sympathetic fluctuations. What wireless is to telegraphy, these sympathetic forces are to the general market price changes.

It appears reasonable that prices should rise and fall directly as the result of changes in the relationship of supply and demand, both of the commodities themselves and of real or possible substitutes. Bread prices rise because the price of wheat has risen, due to a shortage in supply. The price of potatoes increases because of a poor crop, and rice increases in price because of a demand created by a potato shortage. Shoes are dearer because leather is scarce; clothing is higher because cotton, wool, and dyes are up. But just because these things have increased in price is no reason why brooms should suddenly leap up 35 or 40 cents, or why coffee, tea, and cocoa should rise, or why the price of bananas should go up.

Sympathetic price changes are psychological. The higher price of commodities, driven up by a shortage of supply, breaks through the established system, and paves the way for all commodities. Shortages are talked about everywhere, until things are "expected" to be higher in price. Middlemen are not slow to take advantage of such a condition in the public mind. To them it is a part of demand and supply.

**164. The "Spread."**—Considerable interest has been manifested, in late years, in the margin between the price paid the producer and the price charged the consumer. This margin is called the "spread." It has been estimated that the producer of farm products gets from 33⅓ per cent to 47 per cent of the consumer price. An expert testified recently that in former years, "a four-cent hog gave a nine-cent pork-chop; now an eight-cent hog gives an eighteen-cent pork chop." The accompanying table from official sources illustrates the "spread" between the price of wheat to farmers and the price paid by consumers for flour.[13]

COMPARISON OF PRICE PAID FARMERS FOR WHEAT AND PRICE PAID BY CONSUMERS FOR FLOUR, MARCH AND OCTOBER, 1906, 1910, AND 1911

| Item | 1906 | | 1910 | | 1911 | |
|---|---|---|---|---|---|---|
| | March | October | March | October | March | October |
| Average price per bushel paid farmers for wheat of all grades delivered at 10 elevators...... | $0.640 | $0.561 | $0.950 | $0.842 | $0.792 | $0.978 |
| Average retail price of 49 lb. of flour as sold in 48 and 49 lb. sacks by 34 retail merchants: Including value of sack..... | 1.226 | 1.127 | 1.575 | 1.518 | 1.437 | 1 507 |
| Not including value of sack.. | 1.176 | 1.081 | 1.520 | 1.465 | 1.387 | 1.460 |
| Average retail price of 34 84 lb. of flour assumed as the product of 1 bu. of wheat (computed from sales in 48 and 49 lb. sacks, as reported by 34 retail merchants) value of sack not included.................. | .836 | .769 | 1.081 | 1.042 | .986 | 1.038 |
| Excess of retail price of 34.84 lb. of flour assumed as made from 1 bu. of wheat over elevator price of 1 bu. of wheat........ | .196 | .208 | .131 | .200 | .194 | .060 |

The Federal Trade Commission found by investigation that Boston coal dealers, who paid $6.65 in April and $6.75 in May, 1917, for anthracite coal, sold it "almost uniformly" at $9.50 per net ton.[14]

The war has largely unsettled these margins. In such a situation, the unscrupulous dealers will take advantage of the defenseless public to profiteer. "Society has permitted large margins for a marketing cost and now society is investigating to see how this margin is used."[15]

**165. Price Fixing.**—To prevent a disruption of the market, the government decided during the war to control the

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[13] U. S. Bureau of Labor Statistics, Bulletin No. 13a, p. 4.

[14] *Official Bulletin,* August 27, 1917, p. 9.

[15] S. O. Martin, *Annals of the American Academy of Political and Social Science,* May, 1915.

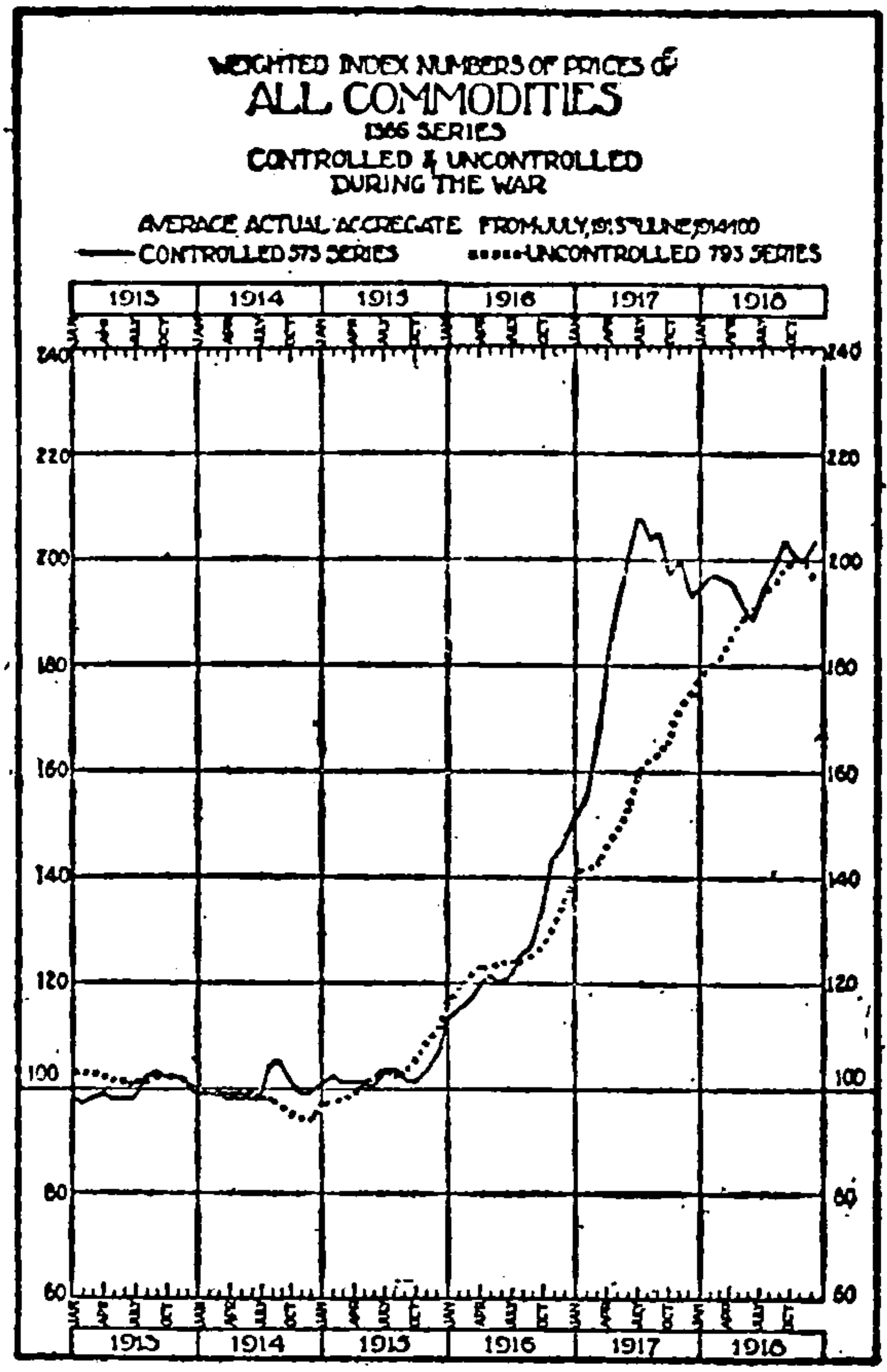

CHART SHOWING THE EFFECT OF PRICE FIXING DURING THE WAR

prices, at least of the essential commodities. A minimum price was guaranteed for wheat; a margin of profit was set for the meat packers; wholesale prices were published and retail prices were "suggested"; the price of pork was tied up with the price of corn; the price of milk was fixed at "the cost of production plus a reasonable profit." But not all commodities were controlled and a comparison is thus posible to show the relative movements. The accompanying graphs afford this comparison, as well as the relation of foodstuffs to "all commodities."[16]

**166. Fair Price.**—Much has been said recently about a fair price. The question always comes forward prominently

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[16] Mitchell, *op. cit.,* Summary, p. 47.

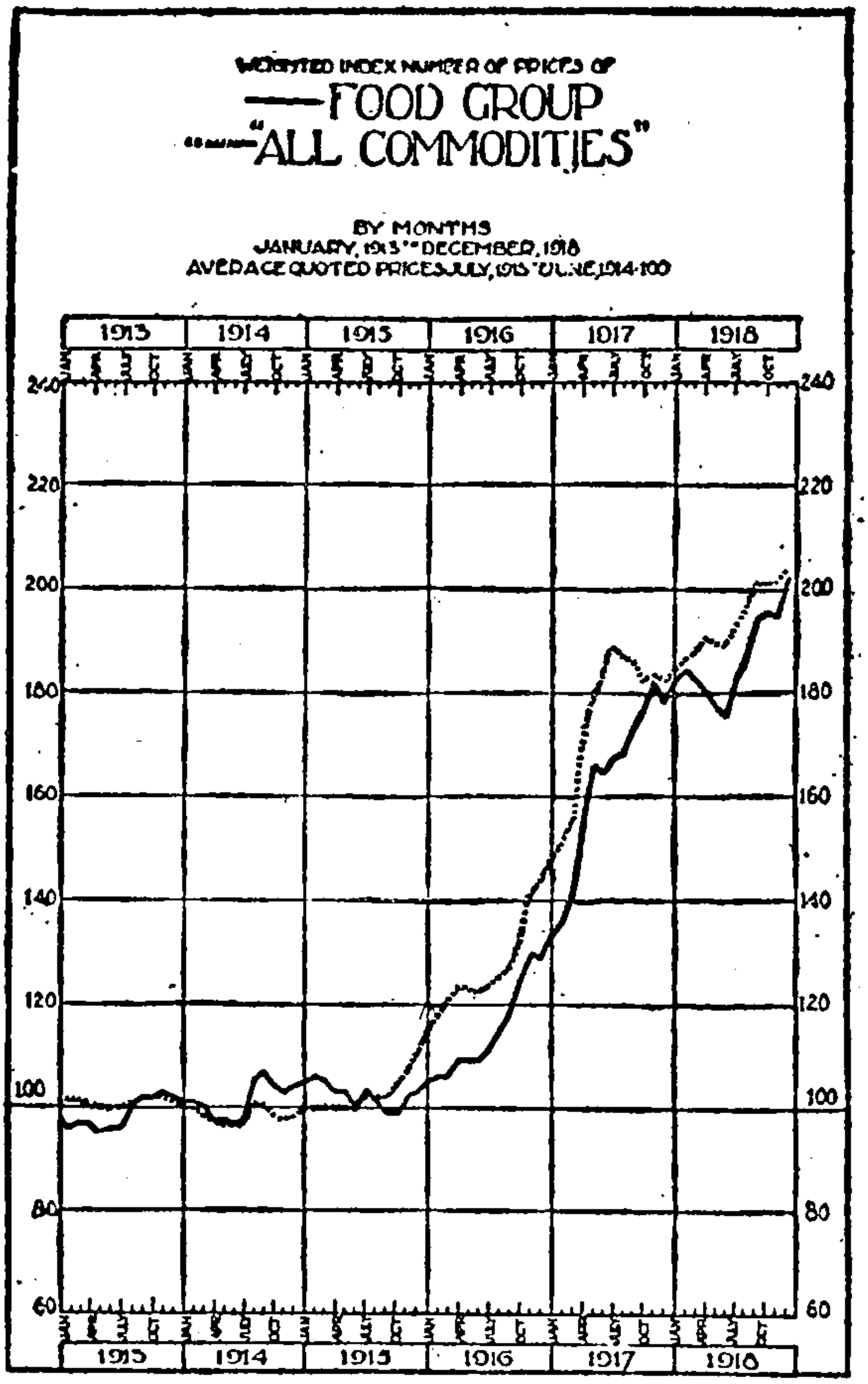

CHART SHOWING THE EFFECT OF PRICE FIXING DURING THE WAR

as prices rise. No satisfactory answer has been given, however, and the subject is as confused as ever. Probably the most widely accepted principle by which prices were set, during the period of their control, was cost plus 10 per cent profit. From a broad social point of view, a fair price is one which will call forth sufficient production and at the same time permit adequate consumption. Practically, there must be such an adjustment of prices that the masses of people can buy a sufficient amount of the necessaries of life. If they must economize to the point of keen deprivation, there will arise resentment at an unjust price system, whatever the causes. Fair price is the result of an attitude of mind; one which results from a feeling of general well-being.

**167. Prices and Costs.**—Practically, as well as theoretically, the minimum of prices for a long period is cost. This principle holds true for handling goods just the same as for producing them. The charge for transportation, for example, has as a minimum the actual cost, and for a maximum a vaguely determinable rate called "what the traffic will bear." The analogue of this minimum and this maximum runs through all prices.

Men do what pays them best. All middlemen want to handle those goods that carry the largest margins between cost, including expenses of handling, and the selling price. They may refuse to distribute commodities which will not pay a return above cost that is sufficiently attractive. Fruit has been left to rot in Michigan orchards because the Chicago market would not absorb it at a satisfactory margin. Just as the producers demand a satisfactory return for an adequate supply, so the middlemen demand a satisfactory return for distributing commodities.

## SUGGESTIONS FOR STUDY

At this point the student should study the price problems connected with his special commodity. For classroom work the following points will serve for discussion. The readings given below should be assigned as a background for discussion.

1. Market price as a focus of economic forces.
2. Price index numbers.
3. Forecasting prices.
4. Scientific method of price quotation.
5. "All economic purposes and methods take on the price emphasis. Price becomes the central and pivotal fact in all industry and business. The theory of price is

thus the core of all economic theory. The rest is corollary or application."

6. Trace the relation between (*a*) production, (*b*) wholesale price, and (*c*) farm price of some commodity.
7. Dominating factors in price.
8. A basic price.
9 Price quotations and actual sales.
10. The price system.

READINGS:

U. S. Department of Labor, Bureau of Labor Statistics, Whole No. 114, p. 22;
——Whole No. 181, pp. 34-8, 110-17;
——Whole No. 130;
——Whole No. 134.
Huebner, *Agricultural Commerce,* Chap. XVII.
Weld, *Marketing of Farm Products,* Chaps. XII, XIV.
Copeland, *Business Statistics,* pp. 53-97.
Wiest, *Butter Industry in U. S.,* Chap. VII.
Adams, *Marketing of Perishable Farm Products,* Chap. II.
*Annals of the American Academy of Political and Social Science,* September, 1911, pp. 155-188.
Todd, *The World's Cotton Crop,* Chap. VIII.
Mitchell, *History of Prices During the War,* "Summary" (this entire series should be available).
Holmes, "Cold Storage and Prices," U. S. Department of Agriculture, Bureau of Statistics, Bulletin No. 101.

# CHAPTER XIII

## FINANCING DISTRIBUTION

**168. The Relation of Finance to Marketing.**—In marketing as well as in production, the problem of financing is a pervasive one. At every step of the way from source to consumption, the commodity is a financial burden on some one. Financial responsibility is the essence of risk in marketing. In order to perform this financing function there has been developed not only the cash banking system but also a remarkable credit system, by means of which charges are piled up against the goods themselves. It is true in a very real sense that commodities are in many cases compelled to furnish their own finances.

It does not lie within the scope of this discussion to explain the organization of banking or the methods of banking. The relation of finance to the marketing problem is, however, necessary and essential to an understanding of a very important phase of the subject. In the first place, commodities may be used as collateral, that is, as security, for borrowing money, and there must be, for good business practice, a document to identify the responsible party. The plan to be followed in this discussion is to define the various methods of sale, and then to take up in detail the chief credit instruments, such as the check, the bill of exchange, the bill of lading, the warehouse receipt, and the trade acceptance.

**169. Methods of Sale.**—Commodities are usually sold in the local market on a cash basis. There is the well-known seasonal strain upon the financial system to concentrate sufficient funds in the grain-growing regions. It may be that some local merchant, banker, or dealer will give credit on a growing crop of cotton, grain, or other produce, or on a herd of cattle. In the latter case, "loans made by cattle-loan companies are divided generally into three classes. These comprise: (1) feeder loans, (2) stocker loans, subdivided into loans on cows, loans on young stock, and 'summer loans,' and (3) dairy loans."[1] This operation is, however, analogous to loans to manufacturers and is not essentially a marketing problem. Coöperative companies may settle periodically. It may be said, in general, nevertheless, that the local-market sale is a cash sale.

When commodities are sent to the primary market there are several types of sale. (1) They may be consigned to a commission man, broker, or, as in the case of cotton, to a factor. In this case, the middleman who receives them waits until they are sold by him before settling, and then after deducting his fee, transportation charges, and other cost, remits the balance to the shipper. (2) Shippers may run an open account system, collecting periodically. (3) Goods may be shipped with a draft attached to the bill of lading, and payment must be made to a bank who handles the transaction. (4) Prices may be made f.o.b. destination or shipping point. (5) The condition of sale may include all payment for transportation and delivery, and is known as "delivered" sale. (6) Sales may be made on the basis of a previous contract. (7) Sales may also be made through an auction, generally known as "auction," to distinguish it from "private," sale.

Credit plays a very large part in the wholesale market sales. It has been estimated that more than 90 per cent of the wholesale transactions involve some kind of credit instruments. Here, then, the next problem of financing arises. In the use of the credit instruments, who has the advantage? Does this method place the control of the goods more or less quickly into the hands of the middlemen? Do these instruments serve the best interests of producer, middleman, retailer, consumer?

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[1] ——— *Journal of Political Economy,* vol. xxvi, p. 810.

Between wholesaler and retailer there is also an extended use of credit instruments. One important function performed by the wholesaler is to aid the retailer financially. A great many methods are used here. It is the field for the operation of the trade acceptance. The bill of exchange is also frequently used. In general, the aim is to make the goods responsible for the financial obligation, payment being made as the goods are sold. This is the field for the credit man.

There are, then, two methods of sale, for cash and on credit. Banks must stand behind both of these methods. In the former, the deal is speedily closed; possession and title pass from producer to middleman at once; full responsibility is transferred. In the latter case, the deal is prolonged, is more complicated, and creates numerous problems. These can best be studied through the credit instruments themselves.

**170. The Check.**—The most familiar credit instrument is the check. It is a demand note, payable at sight, and is most serviceable to save the actual handling of cash. When the necessary relationship between buyer and seller is established, it is a convenient means of facilitating a transaction. There is no need to discuss it in its various forms; the chief inquiry to make is about its negotiability. When this is established the check can readily take the place of cash. Gradually it is displacing the use of cash in the local markets as the producers are being educated to appreciate its convenience. It serves so well as a receipt, in addition to being a medium of exchange, that prejudice only will limit its use. "We are justified in concluding that 50 or 60 per cent of the retail trade of the country is settled in this way. Over 90 per cent of the wholesale trade of the country is done with checks and other credit documents. We may therefore safely accept an average of 80 to 85 per cent as the probable percentage of business of this country transacted by check.''[2]

**171. Bill of Exchange.**—In general, a bill of exchange is an unconditional order signed by one party, the drawer, upon another, the drawee, to pay on demand or at a specified or definite future date, a sum of money to bearer or to a third party, the payee. It is the custom for the drawee to indicate his willingness to pay, that is, he ''honors'' the draft, by writing across the face of it the word ''accepted.'' According to whether or not the bill of exchange has to do with parties living in the same country or in different countries, it is called a domestic bill or a foreign bill. Practically no distinction is made between a draft and a bill of exchange; the words refer to the same type of instrument.

Bills of exchange may be drawn by one banker upon another; these are called banker's bills, or finance bills. They also may arise out of a commercial transaction; these are called commercial bills. It is the latter class that is of particular interest here. Commercial bills represent credit granted against the goods, as well as upon the responsibility of the party who accepts. Accommodation bills and promissory notes are not considered.

The person upon whom the commercial bill of exchange, or draft, is drawn is, generally speaking, the purchaser of goods, or his agent or representative. It is immediately clear that the draft is used to facilitate long distance transactions. The seller of goods needs quick payment, in order that he may carry on business continuously; the buyer may need to borrow money on the goods sent, to be repaid as they are sold. Both the seller and the buyer look to the banker. For the required loan, the banker needs security. The mechanism for facilitating the loan is the bill of exchange, and the security is the bill of lading which carries title to the goods. On a part of the way these two documents go hand in hand; the draft reaches the banker with the bill of lading and other documents attached.

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[2] Quoted in Moulton, *Principles of Money and Banking,* p. 37.

The documents that are attached to a draft are, in domestic trade, the bill of lading, the insurance certificate, and, frequently, the invoice. Other documents such as customhouse receipt, consular invoice, are employed in foreign trade. Usually the draft moves "documents against acceptance," which means that the documents attached to the draft are sloughed off when the drawee has accepted it, and are given to the consignee thus enabling him to obtain the goods. The bill of exchange then becomes a "clean" bill; the indebtedness arising from the transaction no longer runs against the goods, as between buyer and seller. It now becomes a banking problem.

Drafts, especially in foreign trade, are sent in duplicate. The documents are made out at least in triplicate and sometimes as many as ten copies are made. An example of a bill of exchange, original and duplicate, is given herewith.

Drafts are sent usually to banks for acceptance. In handling drafts, endorsements are necessary the same as with checks. Financial arrangements have, of course, always been made previously with the drawee for the acceptance of drafts. This, however, is also a banking problem and is an illustration of how important is the banking system in financing the marketing.

It is important that drafts should be readily negotiable. In order that a draft may be received without question it must not only be properly drawn, but also, through endorsement and acceptance, the full and clear liability of a responsible party must be established. Personal liability

Exchange for
£4326=10=5
Chicago Apr 27 1916
Sixty days after sight of this FIRST of Exchange (Second of same tenor and date unpaid)
Pay to the order of [redacted]
Value received and charge the same to account of value received
To Messrs T. J. Burns & Co Ltd
Queen St
Liverpool
No
E. G. Powell & Co
per:- Powell Pres
FORT DEARBORN NAT'L BANK CHICAGO, ILL.
REPORT BY THIS No. 90457 B/C
Documents to Payment.
S.D. Childs & Co 136 So Clark St. Chicago

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Exchange for
£4326=10=5.
Chicago April 27 1916
Sixty days after sight of this SECOND of Exchange (First of same tenor and date unpaid)
Pay to the order of [redacted]
Value received and charge the same to account of Value received
To Messrs T. J. Burns & Co Ltd
Queen St
Liverpool
No
E. G. Powell & Co
per:- Powell Pres
FORT DEARBORN NAT'L BANK CHICAGO, ILL.
REPORT BY THIS No. 90457 B/C
Documents to Payment.
S.D. Childs & Co 136 So Clark St. Chicago

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Pay to the order of
Fort Dearborn Natl Bank
Chicago
E. G. Powell & Co
per:- Powell
Pres

PAY TO
LLOYDS BANK, LTD.
OR ORDER
PRIOR ENDORSEMENTS GUARANTEED
FORT DEARBORN NATIONAL BANK
CHICAGO
MANAGER FOREIGN DEPT.

Pay to the order of
Fort Dearborn Natl Bank
Chicago
E. G. Powell & Co
per:- Powell
Pres.

PAY TO
LLOYDS BANK, LTD.
OR ORDER
PRIOR ENDORSEMENTS GUARANTEED
FORT DEARBORN NATIONAL BANK
CHICAGO
MANAGER FOREIGN DEPT.

BILL OF EXCHANGE, WITH ENDORSEMENTS ON BACK must take the place of marketable commodities. These goods are then free to enter the market for sale.

Drafts are used in selling goods to wholesale merchants and in sales by wholesale merchants to the retail trade. In foreign trade the use of drafts is the generally acceptable method of financing. In domestic trade there has been an obstacle to its general use by the rather widespread feeling that a draft drawn "against document" or "against payment" is an unwarrantable method of "dunning" the purchaser. Abroad this form of credit instrument is used more widely.

**172. Bill of Lading.**[3]—Among the multifarious business forms used by the railroads is the bill of lading. This is a very important instrument now and has manifold possibilities for future development. It has been estimated that annually there is about $25,000,000,000 worth of business handled through bills of lading and of that $5,000,000,000 is handled by the banks. It is no wonder, then, that much concern is felt about the liabilities and conditions connected with the bill of lading. What kind of an instrument this bill of lading is, what functions it performs as a commercial document, what steps have been taken to safeguard it and to make it uniform, and under what conditions and regulations it moves to-day will be discussed here.

The bill of lading should be sharply distinguished from other forms associated with it. The freight bill, or the shipping bill, is a receipt for the goods delivered to the carrier, and nothing more. It is a form developed to fulfill that specialized function out of which the bill of lading grew. The bill of exchange, to which the bill of lading is often attached, as has been shown, is an independent, although interrelated, document.

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[3] The substance of this discussion is taken by special permission from an article by the writer published in the *Journal of Political Economy,* vol xxv, pp. 679-703.

As a mechanism for facilitating the transportation of goods, the bill of lading has three functions to perform. One of these functions is to serve as a receipt for the goods, in which it duplicates the work of the freight bill. Indeed, it is gradually transplanting that document, just as the check is displacing the formal receipt in general mercantile transactions. A second function is to serve as a written evidence of a contract of shipment between shipper and carrier. A third function is to serve as a document of title to goods. In one or the other of these functions the bill of lading meets the needs of four parties chicfly concerned with a shipment of goods, *i.e.*, the shipper, the carrier, the banker, and the consignee.

Bills of lading also fall into various groups or classes, according as they are looked at from different angles. First, as to kinds of freight, the bills fall into two groups. There are those intended to apply to general merchandise, which may be grouped into one great class. The second kind may be called commodity bills, such as those intended for the conveyance of livestock, grain, cotton, and perishable produce. These are generally known as grain bills, cotton bills, and so forth. Again, bills of lading may be classified, on the basis of the maker, into those issued by a firm or corporation or individual—a private bill—and those issued by the carriers themselves. In another way, they may be arranged on the basis of the factors effecting negotiability into *order* bills and *straight* bills. The former are those which may be transferred by indorsement, the latter are those accompanying the goods consigned directly to consignee and are merely assignable. And, finally, on the basis of the "conditions" of the contract of carriage, the stipulations and the limitations of liability, and the agreements with connecting lines, there are the standard (or

Revised Bill of the Southern Classification Territory), the uniform, the through, and export, and the special bills. The last-named are distinct as being issued under common-law liability.

For several years there was a movement to make bills of lading uniform throughout the country, both as to the law under which carriers operate and as to the conditions of the contract of shipment. This question of uniformity resolves itself into an attempt to harmonize the interests of the four parties chiefly concerned in the transportation of commodities. The shipper, in sending forth his goods into distant markets, is desirous of ridding himself as quickly as possible of all responsibility for them and, at the same time, of being able to realize as quickly as possible on the deal. He is anxious to have his goods arrive as speedily and safely as possible and to have his customer accommodated as completely as possible with the least possible expense. That is, the shipper insists upon as much service from the carrier as he can get for the transportation charge. Opposed to these interests of the shipper are those of the carrier, who naturally wants to assume as little responsibility as he can. One fundamental issue arises out of this clash of interests—where shall the carrier's duty and liability begin and where shall they end?

On the financial side, too, an issue appears. Here the interests of the shipper, the carrier, and the banker are involved. It has been said that the shipper wants to be able to secure speedy reimbursement. For this he appeals to his banker, who says that he is willing to finance the transaction for a fee, provided his own interests are safeguarded. This means that there must never be any doubt of the documents accompanying the bill of exchange, and this means that always the liability on the bill of lading shall be sure and definite. To what extent, then, can any doubt as to the validity of the bill of lading arise, and what is the status of liability?

As for the consignee, his interests in the bill of lading, while not identical with, aid and abet those of the shipper. Just as the latter wants the goods delivered so as to accommodate the consignee with least expense, so the consignee wishes to get as much service, in addition to his goods, as he can. Both shipper and consignee try to shift the burden onto the carrier. In his relations with the banker the consignee again joins with the shipper in asking for financial facilities. Often, of course, the consignee pays the freight and in such a case becomes the shipper. There is, therefore, no new issue developed out of these relations.

The two most important interested parties from the marketing point of view are the shipper, who is usually the seller, and the consignee, who is usually the buyer. The typical shipper represents the merchant function in modern business. His immediate and ever-present concern is to have his goods available for as wide a market as possible at least expense. The common carriers have made possible for him a world-wide market, so that he sells to buyers whom he has never seen, goods which they have never seen. No matter whether this shipper is large or small, whether he has his own sidetrack or hauls his goods to the freight station, whether he loads his own cars or those of the railroad, he loses control and care of his goods when they start forth on their journey. So dependent has he become on this common carrier that he feels his responsibility ended when the goods, as ordered, are delivered to the railroad. All he asks in return is some indubitable evidence to serve as a receipt as to the character and amount of goods shipped, and by means of which he can pass title. The shipper then turns his attention to getting his money out of the deal as soon as he can.

The typical consignee is the purchaser of goods f.o.b. destination. He has bought goods which he has never seen, from a distant seller whom he may never have seen. His first interest is in the integrity of that distant seller, for he wants to be confident that the goods are of the character and quantity bargained for. He leaves it to the seller to arrange for the arrival of the goods. But from the carrier he expects assurance that the goods are as represented in the bill of lading; he expects a check on the integrity of the seller, for the carrier gives a receipt at the shipping point and therefore has the mechanism for checking up this matter. The consignee will therefore insist that the carrier be held responsible for the face of the bill of lading signed by its agent. Aside from this the consignee expects from the carrier an efficient fulfillment of the carrier function, *i.e.*, speedy and safe transportation and the prompt notification of the arrival of the goods. On his part, too, he must be ready to receive the goods and, when title passes to him with the possession of the bill of lading, to assume his responsibility for them. The point at which this responsibility passes from the carrier to consignee must be specifically ascertainable.

The so-called Pomerene Bill, which became a law on August 29, 1916, and went into effect January 1, 1917, has established a uniform bill of lading throughout the country. A very great deal was said at the hearings on this Bill about making a bill of lading more worthy of its position as an important document by means of an increase of its negotiability. Says one witness, Sol. Wexler, Vice-President of the Whitney Central National Bank, New Orleans, La.:

> I maintain that the business of the world, not only of the United States, but of the whole world—as it is done to-day—is done largely upon bills of lading, whether "to order" or

> "straight"; that it has become the most important instrument of credit in use in the world to-day of any kind; and that it is necessary for the commerce of this country to make that bill of lading fully negotiable, entirely safe, and to make the person who receipts for the goods, whether they have been delivered to him or not, responsible for their delivery. . . . All we are asking of this bill of lading is to protect the innocent holder of the document.[4]

And also, as phrased by Francis B. James, the leading advocate: "An order bill of lading is commodity currency, and is doubly so when accompanied by a draft—the draft with its dollar mark representing the unit of value and the order bills of lading a unit of quantity. By the use of a negotiable order bill of lading, properly protected by legal sanction, our great staples and other commodities are turned into a part of the asset currency of the country."[5]

As illustrated by these quotations, two main requests stand out from the discussion. One is that the liability on bills of lading be readily ascertainable from those instruments themselves, and the other is that the bills be made more fully negotiable. Incidentally it is suggested that the liability be defined, so as to hold the carrier more fully than formerly. This position would be enough in itself to range the shippers, receivers, and bankers on the one side of the question. But these two points are not independent of each other. Clearly defined liability on the part of the responsible party is an essential to free negotiability. Therein may lie another reason for holding the carrier to more extended liability.

Something further needs to be said about the negotiability of the bill of lading. Extravagant and not well-considered statements have been made on the subject. "The bill of lading," wrote President Hadley years ago, "is made to serve the same purpose as a bill of exchange."[6] "The (order) bill of lading thus contributes to that fluidity of the circulating medium, that celerity in the transfer of merchandise, which are striking achievements and essential requirements of current civilization."[7] "Bills, drafts, notes, checks, and bills of lading are in fact and practice parts of the currency of commerce."[8] "A negotiable order bill of lading ought to be as clean as a check, draft, or promissory note."[9] What specifically can these utterances mean? Apparently the idea that lies behind them is that bills of lading may be made into a new kind of currency of commerce, so that they may save "the necessity of the large concentration of money to handle and move the staple commodities of the country."[10]

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[4] Hearings, 61st Congress, 2d Session, p. 40.

[5] *Ibid.*, p. 55.

Such a service is demonstrably impossible. Not only are bills of lading representative of a unit of quantity, of a certain amount of certain commodities—and commodities for obvious reasons can never again become a universally acceptable medium of exchange—but they also are not used or intended to be used, as a medium of exchange, as the currency of commerce in any true sense. Negotiability, as used in relation to bills of lading, does not, or should not, imply making them serve the purpose of bills of exchange. The distinction was correctly stated, though for a different purpose, by W. W. Porter many years ago:

> A large number of dicta have been uttered by eminent authorities in assertion of the negotiability of the bill of lading, but no case can be found, unless arising under a special statute, in

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[6] *Railroad Transportation*, p. 58.

[7] McPherson, *Railroad Freight Rates in Relation to Industry and Commerce*, p. 190.

[8] *American Uniform Commercial Acts*, p. 56.

[9] *Ibid.*, p. 20.

[10] Hearings, p. 15.

which a bill of lading has been treated as an instrument which is negotiable in the same sense as bills of exchange and promissory notes are negotiable. All broad assertions of the negotiability of the bill of lading, when examined in the light of their context and of their actual application to the very cases in which they were unguardedly made by the Court, will be found equivalent merely to a statement that the bill is transferrable by indorsement and delivery and that such indorsement and delivery transfer to the indorsee or holder such rights to, or property in, the goods as it was the intention of the parties, gathered from all the circumstances, to pass.[11]

Bills of lading are not currency any more than mortgages and deeds and warehouse receipts are currency. They are collateral security and nothing more. Nor will it ever be possible for them to meet the requirements of the true negotiable instrument. An instrument to be negotiable must conform to the following requirements: (1) it must be in writing and signed by the maker or drawer; (2) it must contain an unconditional promise or order to pay a certain sum of money; (3) it must be payable on demand, or at a fixed or determinable future time; (4) it must be payable to order or bearer; and (5) when the instrument is addressed to a drawee, he must be named or otherwise indicated therein with reasonable certainty.[12]

Requirement (2) makes the vital and essential distinction between bills of lading and bills of exchange or promissory notes. And a use of the words "currency of commerce" in connection with bills of lading or a classification of them indiscriminately with checks, drafts, and notes is confusing and misleading.

The Pomerene Law has not, therefore, made the bills of lading "currency of commerce" or capable of taking the place of bills of exchange. It has, however, done a good and great service; it has clearly defined the responsible parties in the shipment contract and thereby has made the bills of lading more readily acceptable as collateral security for loans by means of bills of exchange. This is true both for "order" bills and "straight" bills; and this was and should have been the essential purpose of the law. The negotiability of order bills readily follows under the provisions permitting transfer of title.

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[11] *The Bill of Lading,* p. 79.

[12] Uniform Negotiable Instrument Law, Sec. 1.

But in extending the liability of carriers something else also resulted. The carriers were forced to become a kind of "guaranty trust company." In practice, bills of lading are not made out by the carrier's agents in the vast majority of cases.

> To-day I think it is no exaggeration to say that not one bill out of a thousand—and I believe I could say 10,000, is made out by the agent of the railroad company. The business of this country could not move for a single day if the bills of lading were not made out by the shippers. It is not merely a question of the number of agents or the size of the platforms to hold freight, but it is a question of time. There are not enough hours in the day, and there is not enough space in the streets of any large city adjoining the terminals of railroads, to accommodate the drays and wagons. . . . That bill of lading is checked with the goods, if there is time. If there is not time, it is checked with the shipping order. . . . The main object in life is to get rid of that drayman.[13]

This law compels responsibility by the carrier on bills filled out by the shippers, hastily checked by the agents of the carriers, and then signed. Bills of this character are to be raised to a plane of unquestioned reliability. The railroads claim, and with a very sensible show of justification, that a careful checking up on these bills is necessary for such liability; that this is a new and expensive service not included in the present rates charged; and that an added recompense is due them for it.

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[13] Hearings, 61st Congress, 2d Session, p. 101, testimony of H. L. Bond, general counsel of the Baltimore and Ohio R. R.

The Pomerene Law, then, has favored the shipper, the receiver, and the banker by giving a better kind of collateral security, upon which bills of exchange are more confidently drawn and more readily accepted. This has certainly facilitated commerce, has made bills of lading better commercial paper. At the same time, in extending the liability of the carriers, it has compelled them practically to guarantee the integrity of shippers who make out their own bills of lading, and to be responsible for the acts of all their agents, near and far, high grade and low grade, contrary to the decision in the Friedlander case. Furthermore, it has declared the negotiability of order bills and the transferability of straight bills. The broad lines of liability are thus uniformly laid down.

It may be deduced from these considerations that the bill of lading can never become a negotiable instrument "ranking on par with a bill of exchange," because their functions are different in character and because the word "negotiability" cannot be applied in the same sense to both of these instruments. Furthermore, it seems clear that three different functions have been concentrated in this bill of lading, namely, to act as a receipt, as a contract, and as a document of title to goods, and that the movement for uniformity, by extending the carrier's liability, has added a fourth as a guaranty of the shipper's integrity to the banker and the consignee. That these functions are merged one into the other by practical considerations is manifest. Some careful thinking and some clear reasoning will be needed to disentangle them. And shooting through all these problems is the practical issue—traffic must move. It is that issue which sets the bill of lading apart from other similar documents, such as deeds, mortgages, and warehouse receipts, important as they are.

And, lastly, this discussion has revealed the great importance attached to the bill of lading as collateral security. When the bill of exchange, with documents attached, moves "documents against acceptance," the bill of lading assumes transcending importance; it must be unquestionable security. This is true in both domestic and foreign trade. This piece of commercial paper, issued annually to an extent that represents twenty-five billion dollars worth of commodities, is a commercial instrument worthy of much serious consideration.

"The bill of lading is an instrument for facilitating commerce, the importance of which is not generally known."[14] It will never fully come into its own until all controversies concerning interpretation, responsibility, and liability are adjusted. Toward this adjustment great strides have been made. All interested parties have been heard; the evidence is in; uniform laws are being adopted in one state after another; the "conditions" alone are under fire. The decision of the Interstate Commerce Commission on these disputed points is due.

**173. The Warehouse Receipt.**—When goods enter a warehouse, of whatever character, the warehouseman should issue to the owner of the goods a receipt for them. This receipt is called a warehouse receipt. For goods in foreign or interstate commerce a warehouse receipt is required under section 17 of the U. S. Warehouse Act, June 30, 1917.

> Sec. 17. That for all agricultural products stored for interstate or foreign commerce, or in any place under the exclusive jurisdiction of the United States, receipts shall be issued by the warehouseman conducting the same, but no receipts shall be

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[14] McPherson, *op. cit.*, p. 190.

issued except for agricultural products actually stored in the warehouse at the time of the issuance thereof.

It is required under this Federal Warehouse Act that every receipt shall embody the following points: location of the warehouse; date of issue; consecutive number; to whom deliverable; rate of storage charges; description of products, together with quantity and, in the case of packages, the usual marks and weights; grade, or other class stated in Federal grades if so fixed by law, and otherwise the recognized standards to be used, issued under U. S. Warehouse Act; interest of warehouseman if any; statement of advances and liabilities for which warehouseman claims a lien; such other items and conditions required by law as signature of warehouseman and, if not negotiable, without mention of grade or class.

It is important to distinguish between negotiable and non-negotiable warehouse receipts. To be negotiable a receipt must state either that the goods received and stored under it will be delivered to the bearer, or that they will be delivered to a specified person or on his order. The latter type of warehouse receipt, like the check, requires endorsement. A non-negotiable receipt is one which states that the goods stored under it will be delivered to the depositor only or only to a specified person named in the receipt. In this case, the words "non-negotiable" or "not negotiable" should be written across the face.

Neither the bill of lading nor the warehouse receipt can fulfill qualification two prescribed in the Uniform Negotiable Instrument Law, and so cannot be "currency of commerce" in an equal sense with the bill of exchange. If the goods entering storage are merchantable in character and are gradable and carefully graded, there is no reason however why banks should not accept such paper readily up to, say, 20 per cent of the market value of the commodities.

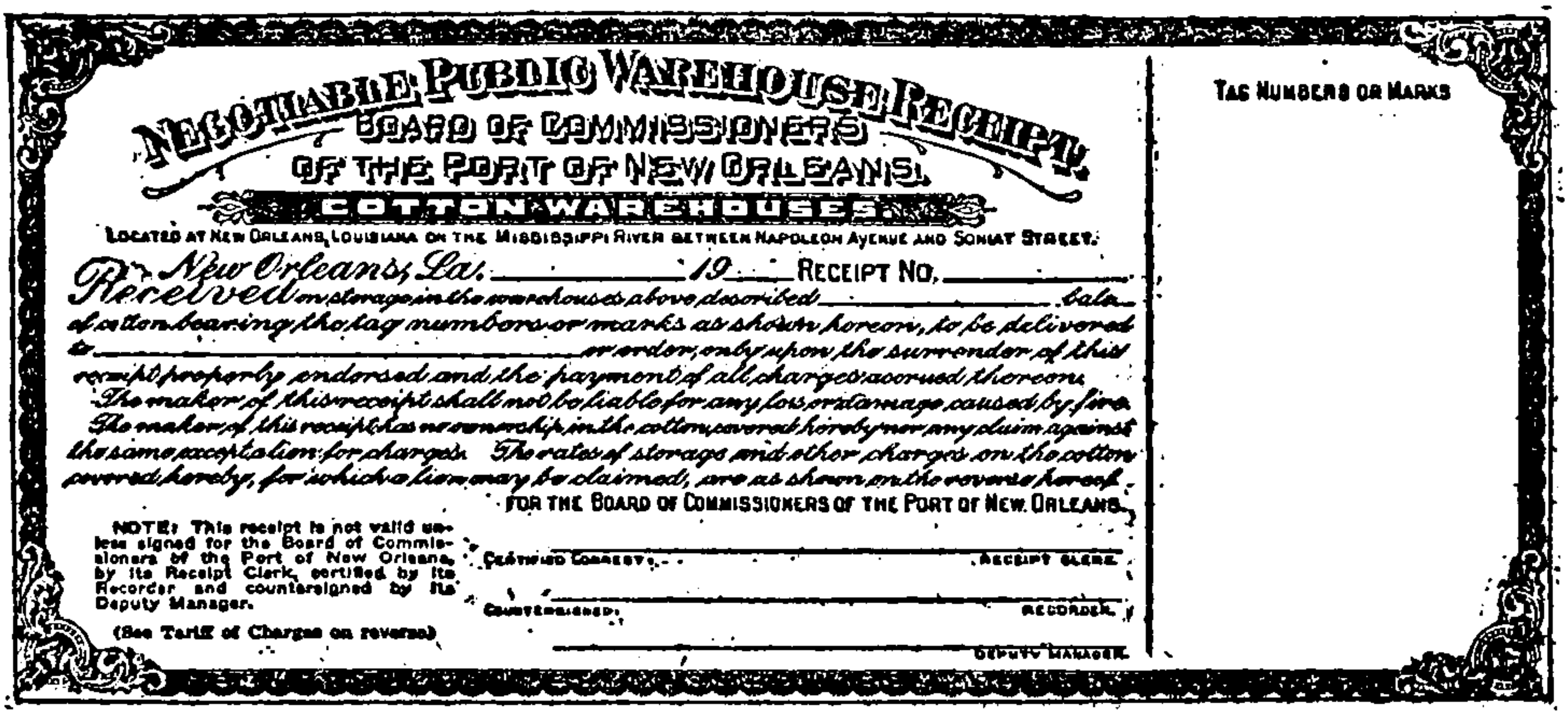
The usefulness of the warehouse receipt is intimately related to grading and prices. A receipt is in reality nothing more than evidence of the existence of a certain amount of goods, of a certain character. This is quite apart from the legal phase. It can be acceptable only on the basis of those goods. No legal-tender notes can be kept at par unless they are always readily redeemable in the universally acceptable medium of exchange. The principle holds for warehouse receipts. Merchandise can never become a rival of gold for a medium of exchange. In so far as there is a difference to the disadvantage of commodities, warehouse receipts will fall below legal-tender notes, checks, and bills of exchange as credit instruments. Warehouse receipts are becoming more widely acceptable as a basis for loans, however, and when better storage methods and sounder, more scientific grades are established their usefulness will increase.

As an illustration of what can be done in extending the use of warehouse receipts, take the following declaration from the Federal Reserve Board, Regulation A, Series 1917, in relation to Section 13 of the Federal Reserve Act dealing with rediscounts of notes, drafts, and bills of exchange. What is true in this particular case will hold true extensively of various kinds of commodities.

> Section VII of this regulation relates to commodity paper, which can be rediscounted for a member bank under the general terms of the regulation, but which may, if it complies with the conditions laid down in this section, be discounted at a preferential rate, which is now 3½ per cent in most of the Federal Reserve districts.
>
> Potatoes, properly graded and packed and stored in a weatherproof and responsible warehouse, as evidenced by its receipt, would undoubtedly constitute a readily marketable, non-perishable staple within the meaning of the regulation. The member bank making loans against warehouse receipts for potatoes

properly insured would, of course, have to satisfy itself as to the margin of its security and the conditions of warehousing, but after having done so, and making the loan, it could rediscount such paper with the Federal Reserve Bank for periods not longer than 90 days.

The insistence upon proper grading, packing, and storing is significant. All of these things have to do with the marketableness of commodities. Some warehousemen guarantee grades, weights, and other essential qualities. Often certain variations are stipulated. But it is clear that the more nearly the guarantee approaches absolute correctness, the more valuable will be the receipt to the person to whom it is transferred. A charge is sometimes made for this guarantee; in cotton, for example, it is usually one-sixteenth of a cent per pound.



NEGOTIABLE PUBLIC WAREHOUSE RECEIPT.
BOARD OF COMMISSIONERS
OF THE PORT OF NEW ORLEANS.
COTTON WAREHOUSES.
LOCATED AT NEW ORLEANS, LOUISIANA ON THE MISSISSIPPI RIVER BETWEEN NAPOLEON AVENUE AND SONIAT STREET.

TAG NUMBERS OR MARKS

New Orleans, La. ____________ 19__ RECEIPT NO. ____________

Received in storage in the warehouses above described ____________ bales of cotton bearing the tag numbers or marks as shown hereon, to be delivered to ____________ or order, only upon the surrender of this receipt properly endorsed and the payment of all charges accrued thereon.

The maker of this receipt shall not be liable for any loss or damage caused by fire. The maker of this receipt has no ownership in the cotton covered hereby nor any claim against the same except a lien for charges. The rates of storage and other charges on the cotton covered hereby, for which a lien may be claimed, are as shown on the reverse hereof.

FOR THE BOARD OF COMMISSIONERS OF THE PORT OF NEW ORLEANS.

NOTE: This receipt is not valid unless signed for the Board of Commissioners of the Port of New Orleans, by its Receipt Clerk, certified by its Recorder and countersigned by its Deputy Manager.

(See Tariff of Charges on reverse)

Certified Correct, ____________ Receipt Clerk.

Countersigned, ____________ Recorder.

____________ Deputy Manager.

WAREHOUSE RECEIPT

A specimen of warehouse receipt is given herewith. It is necessary, of course, to know what charges are running against the stored goods. In the case of this cotton warehouse receipt the storage rates are printed on the back. They run as follows:

### REGULAR STORAGE RATES

| | |
|---|---|
| If received uncompressed, compressed on arrival and stored, first month | 20c per bale |
| If received compressed, first month | 30c per bale |
| Extra storage each additional 30 days | 8c per bale |
| If received uncompressed and stored uncompressed, first month | 35c per bale |
| Extra storage each additional 30 days | 13c per bale |
| Compressing | 40c per bale |
| Fee for tagging, inspecting, sampling, marking, and weighing | 10c per bale |
| Charge for delivering to wharf, railroad, or team | 15c per bale |

A lien is also claimed on cotton covered hereby for any special services which may be performed upon, or for the cotton covered hereby at the request of the depositor or the holders of the warehouse receipt, such as extra weighing, patching, turning out for examination, and other like charges, all in accordance with the regular tariff provided therefor.

**174. The Trade Acceptance.**—"A trade acceptance is a time draft drawn by the seller of merchandise on the buyer for the purchase price of the goods and accepted by the buyer, payable on a certain date, at a certain place designated on its face." The financing of marketing may now be done in either one of three ways: (1) on a cash basis, (2) by open account, (3) by trade acceptances. The open-account basis is peculiar to this country. Following the Civil War financial conditions were so badly disturbed that there were great risks in long-extended credits. In order to induce prompt payments the system of giving discounts grew up. It is to displace this open-account system that trade acceptances are proposed.

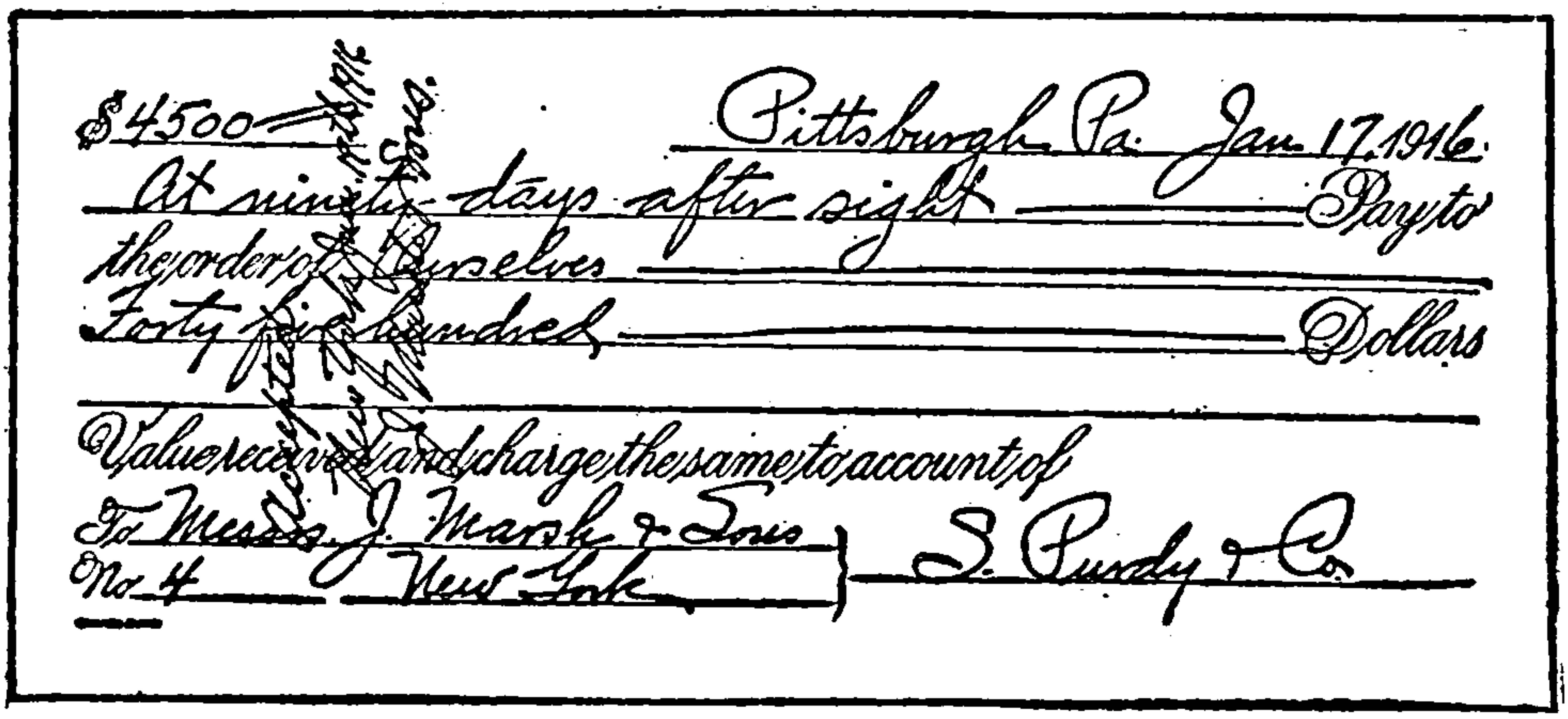
It has been said that the Bank of France handled in pre-war times as much as three billion dollars of acceptances in a single year. The size of these acceptances averaged about $100, and some ran as low as $1. A half billion dollars worth of acceptances were handled by this bank in sums less than $25. In England this credit instrument is in extensive use and is known as a "bill." In Canada it is known as trade paper. Elsewhere its use is an old and well-established system.

Trade acceptances can be used for many kinds of commodities. The Federal Reserve Board has declared that the word "goods" as employed in its definition of a trade acceptance includes goods, wares, merchandise, or agricultural products, including livestock. The time during which the credit instrument runs is usually 90 days or less. It may be taken to a commercial-paper house or a bank and discounted at once or the seller of the goods may hold it in his portfolio until it is nearing maturity and then take it to a bank.

Advocates of the trade acceptance have declared that, while it is not expected to displace all cash sales or all open-account sales, it will be found to be a sounder and safer method of doing business. The acceptance, it is said, is the second line of defense in our banking system, the best assurance against panic, and it is up to the business men of the country to do their part to build up and strengthen this line and make possible to the fullest degree the establishment of a thoroughly scientific banking system. The President of a New York City bank declared, "The trade acceptance is the logical method of conducting the class of business transactions based upon credit. It carries on its face the evidence of efficiency, economy, and security. The trade acceptance means more to the future of American commerce than we can realize at the present."

There are several different kinds of trade acceptances and no definite form should be used without a careful examination. The accompanying example will serve to show the chief characteristics of this form of credit instrument.

The advantages derived from the use of trade acceptances in place of open accounts are claimed to be: (1) to render liquid all slow or "frozen" accounts, (2) to offer a desirable investment by banks, (3) to check overbuying and to strengthen credit among purchasers, (4) to equalize the opportunity for credit between large and small retailers, (5) to make capital liquid, (6) to reduce bad debts, (7) to lower the general cost of financing and (8) to put the credit system on a really scientific basis.



$4500— Pittsburgh Pa. Jan 17 1916.

At ninety days after sight Pay to the order of Ourselves

Forty Five Hundred Dollars

Value received and charge the same to account of

To Messrs. J. Marsh & Sons
No 4 New York
S. Purdy & Co.

TRADE ACCEPTANCE

The primary principle involved here is the same as that underlying the warehouse receipt and the bill of lading. In so far as possible commodities finance themselves. The accumulating charges are secured by the goods. In long distance trading this method eliminates more and more the personal equation that makes open accounts so difficult and unsafe.

**175. Functions of Credit Instruments.**—Business blanks and forms arise to facilitate complex business activities. The more complex, the more far-reaching, and the more impersonal the business activity, the greater the need for these commercial instruments. With the increasing need for such instruments, there is an increasing demand not only for their standardization and uniformity but also for their absolute soundness and security. Credit instruments used in financing the marketing are necessary for long distance and long time dealing. They save the use of actual cash; they greatly expand the service of capital; they are adaptable to a medium of exchange; they become a necessary adjunct to the roundabout process of production; they are practically a prerequisite for speculative business.

As has been shown, the proper form of credit instrument enables the seller of goods to be reimbursed speedily, the risk and burden of expense being transferred to the goods themselves. The buyer also compels the goods to bear their financial burdens largely until they are sold. For a time the carrier, through the bill of lading, shares in the risk and responsibility. All parties finally turn to the banker whose special function it is to afford financial service. Through the entire marketing process, the financing is facilitated by one or the other of the credit instruments indicated here.

## Suggestions for Study

The student should here study the financing problems in connection with his special commodity. This study will be made more concrete if it is made through the medium of actual business forms which can readily be obtained. The following topics will serve for classroom study.

### *Bill of Exchange*

1. Development of the draft.
2. Parties to a draft.
3. Charges on a draft.
4. Negotiability of a draft.
5. Functions of a draft.

### *Bill of Lading*

1. Functions of a bill of lading.
2. Movement for uniformity.

3. Questions of negotiability and liability.
4. Disputed questions under Uniform Bill of Lading Act.
5. Points at issue between shippers and carriers.
6. Commercial importance of the bill of lading.
7. Weak points in commercial use of bill of lading.
8. Future development of bill of lading.

### *Warehouse Receipts*

1. Characteristics of the warehouse receipt.
2. Economic functions of warehouse receipt.
3. Public interest in warehouse receipts.
4. Liabilities on warehouse receipts.
5. Negotiability of warehouse receipt.
6. Interest of producer, shipper, carrier, in warehouse receipt.
7. The receipt and the public warehouse.
8. The receipt and the private warehouse.

### *Trade Acceptances*

1. The trade acceptance and the check, the bill of exchange.
2. Advantages and disadvantages of trade acceptances to buyer, seller, banker.
3. Trade acceptance and risk.
4. Trade acceptance and speculation.
5. Character of goods as affecting the use of trade acceptances.
6. Trade acceptances abroad.
7. Future of trade acceptances.

READINGS:

### *Bills of Exchange*

Escher, *Foreign Exchange.*
Whitaker, *Foreign Exchange.*

### *Bills of Lading*

Bennett, *The Bill of Lading.*
*Interstate Commerce Commission,* vol. xxxviii, p. 91; vol. xli, p. 346.

Porter, *Law of Bills of Lading.*

*American Uniform Commercial Acts,* pp. 14 *et seq.*

Duncan, "Uniform Bill of Lading," *Journal of Political Economy,* vol. xxv, 679-703.

### *Warehouse Receipts*

*Bulletin of American Warehouseman's Association,* November, 1915, p. 357; September, 1916, pp. 282-5; October, 1916, p. 320; February, 1917, p. 47; June, 1917, pp. 190-206; July, 1917, p. 323; August, 1917, p. 257; October, 1917, p. 313; November, 117, p. 341.

*Annals of the American Academy of Political and Social Science,* September, 1911, pp. 281-91.

National City Bank, "U. S. Warehouse Act."

U. S. Department of Commerce and Labor, Bureau of Statistics, Bulletin No. 4, Series 1903-1904, p. 1086.

### *Trade Acceptances*

Mathewson, *Acceptances, Trade and Bankers'.*

Treman, *Trade Acceptances.*

Guaranty Trust Company, "Acceptances" (pamphlet).

National City Bank, "Progress in Development of Trade Acceptances" (pamphlet).

Tingley, *Trade Acceptances vs. Open-Account Credit.*

*How Merchants Can Use Trade Acceptances* (Bernhard and Scholle Co.).

# PART II

# MANUFACTURED PRODUCTS

# CHAPTER XIII

## ANALYSIS OF THE COMMODITY

**176. Differences Between Raw Materials and Finished Goods.**—Production is the creation of value; production adds to economic goods time, place, and form utilities. The creation of time and place utilities is generally the work of middlemen. The creation of form utilities is the work of the manufacturer. As has already been indicated, the fundamental difference, from a commercial point of view, between raw materials and foodstuffs on the one hand and finished products on the other, lies in the fact that the former must be taken as the forces of nature produce them, while the latter can be shaped according to a preconceived plan. In one case there is control of elements that go into commodities and of the form utilities to be created; in the other case this is not true.

This distinction affects the entire problem of analyzing the commodity. In raw materials, the commodities are once removed from human wants; in finished goods the application is direct. In raw materials and foodstuffs the problem is broadly one of supply and demand; in finished goods the problem is one of adaptation and fitness. In raw materials and foodstuffs the task of analyzing the commodity is to study the characteristics and the supply. In finished goods, the problem is one of the historical development, the modifiable qualities in relation to their uses, of supply in relation to the purchasing problem, the stock plan, seasonal buying, etc., of the relation to raw materials, the question of working capital, grading, the possibility of a technical or scientific analysis, and the relation to market demand. The aim of analysis in raw materials is to secure scientific production; the aim of analysis in finished goods is to promote scientific selling.

**177. Historical Development.**—The first logical step in the analysis of a manufactured commodity is to trace the history of its development. Through the years goods have taken on one quality after another to satisfy new wants or to satisfy more completely an established want. An historical background enables the one handling the commodity to find a human interest in many a commonplace thing. For example, there is almost a human touch that makes the whole world kin in the fact that typewriters were first invented for the use of the blind; there was no need, therefore, for the writing to be visible.

The historical survey should include the various steps in the manufacturing process of most commodities. The salesman handling men's clothing should be interested to know that the making of each coat has sixty-four distinct operations and to know what each operation is. The well informed furniture dealer should be interested to know how furniture is made, as well as the styles and the periods of introduction of each. Association and sentiment have much to do with the consumer's attitude toward the pictures and furniture with which he lives, as well as with the literature he reads. The best source for both of these is a knowledge of historical facts. One cannot help having a peculiar interest in the fabric he handles after he has once seen the machines weaving it with almost uncanny skill and intelligence. This is particularly true of the machines that stop when a thread breaks or something goes wrong. One looks with a new interest at the great catalogues put out by one of the leading mail-order houses after he has seen the machines with steel fingers, each reaching out to pick up its quota of pages, and stopping, when a mistake is made, with the steel fingers raised to point the place.

The manager of a large cotton mill, who had come up from the ranks step by step from doffer boy to manager, declared that for him there was no monotony in a cotton mill. He said he knew every machine in the mill; each one had a personality to him. Weaving cotton, he said, is not a commonplace, monotonous job; it is a romance. The humanizing of his engine by an engineer, the loving care of a skilled carpenter of his tools, the devotion of a violinist to his violin, are merely illustrations of a sympathetic attitude that is possible in dealing with almost any kind of a commodity.

Suppose one should undertake a study of the designs of patterns in tapestry, in wall paper, in rugs, in carpets. He would find himself immediately fascinated by the subject. He would be led along strange, alluring paths of oriental mythology, superstition, and religion; he would find himself in the midst of strange phantasy and poetic symbolism. Even the many insignificant notions in the bargain basement can be humanized thus. No commodity passes through the market except to meet some human want. Skillfully or crudely each article has been devised with such an aim in view. Think of the "dinky" steam engines first invented compared with the giant moguls of to-day. Everywhere there are human interest stories in the development of commodities; everywhere there are interesting facts to serve as a background for matching goods to human wants.

Scientific management endeavors to make each job interesting to the worker engaged at it. He is taught to look at the task analytically, to make a study of it, a live problem of it. Thus, his interest is stimulated and sustained. In the historical study of merchandise, likewise, there is the same opportunity. Cotton can be followed from the fields of the South to the finished garment; wool from the ranges to the manufactured article; rubber from plantation, or far-away, strange tropical forests where wild or half-civilized natives exploit it, to the automobile tire; furs from the wild haunts of fur-bearing animals in the North to the gorgeous coat of the rich. There is here no limit to knowledge or to interest. It is the story of the human race wresting a livelihood from a niggard earth.

**178. Philosophical Analysis.**—One may approach the commodity with an abstract or philosophical plan of analysis. The commodity may be taken as a thing apart. From this point of view, any article may be considered, first, as a thing in itself and, second, as to its service in relation to the consumer. When a commodity is considered as a thing in itself, the following queries arise: what the commodity is, of what it is made, for what purpose it is made, historical development, and value. Its service in relation to the consumer involves the inquiries as to whether or not it is for the customer's own use, to be sold by him at a profit, comparison with rival and substitute goods, etc.

In an attempt to put the purchasing for a mercantile establishment upon a scientific basis, it has been suggested that the buying should be done in a "new way." The purchasing agent should first seek all available information in regard to the materials handled, such as sources and volume of supply, graphic record of prices paid in the past, market movements, forecasts of supply in relation to consumption, price fluctuations, product tendencies toward change. There should then be an inspection system, a series of laboratory reports of tests of materials, the behavior of materials in use.

Another method for analyzing has been suggested on the following basis: There are three general considerations, material, commercial, and monetary. Under the material considerations are the properties of the commodity, the appearance, the trustworthiness, the quality, the utility, and the differentiation. Under commercial considerations are the advertisability, depending upon scope of utility; source of commodity; substance of commodity, both tangible and intangible; groups of commodities whether constituent, collective, or integral; classes of commodities, such as novelties or luxuries, necessities, staples; and kinds of commodities, such as meritorious, mediocre, and impractical.[1]

**179. Analysis Dependent on Point of View.**—Naturally the kind of analysis to be made will depend upon the point of view from which the subject is approached. The technical scientific attitude is illustrated by the industrial chemist. The merchant as well as the manufacturer can make use of the chemist, as the following statement shows:

> In the stress of highly competitive production, in the relative scarcity of raw products, in the mounting cost of labor, in the keenness to excel in America's specialty—quantity production, in the very skill of the chemist in evolving substitutes and less expensive ways of doing things—as well as finding better ways of doing things—how can the retailer always be sure that he is getting what he expected—how can he be sure that the merchandise he is selling to his customers will prove to be as represented? And how can the customer know? In the light of modern conditions there is one answer. Only the chemist can tell! The men who work out the secret processes of industry are the only men who can tell or approximate what the result of those processes will do—in terms of health—wear—service. For several years we have not been content to take the word of mill or manufacturer; be they ever so well intentioned—as to whether, for example, a fabric was all wool—or whether it was fast dye.
>
> We have gone to the chemist. And when a fabric was not all wool we have refused to sell the goods; or if cotton really added merit to the fabric, we have not hesitated to say so. We have gone to the chemist for our guidance, in making large

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[1] *Cf.* Wadsworth, *Advertising.*

purchases—for example, of hosiery and other apparel. So that, in addition to the keen eye and sensitive fingertips of the experienced buyer, we added the eternal verity of the test tube and the microscope.[2]

A combined scientific and commercial analysis was made by the manufacturers of a widely-known cooking-fat compound. They had been for years in the business of making and selling a mechanically-mixed lard compound, made up of cottonseed oil and oleostearine. They knew, therefore, the demand for such a commodity and the special qualities required. By means of experiments carried out through a period of four years, they succeeded in producing the right kind of commodity. This task was accomplished by examining all the cooking fats in existence and listing their weak points. Through a process of hydrogenization, they were able to correct such faults as the tendency to become rancid, the large content of stearic acid, the low burning point. Here is an instance where a commodity was deliberately and carefully built up to satisfy an established and well-defined demand.

A retailer, who handles textile goods of various kinds, has advertised that he secured the written opinion of thirty-six experts as to the best way to shrink cloth, in order that his products might thereby be the better. A manufacturer of shoes claims that he has specialists in every branch of the shoe business who make a continual study of factory methods, manufacturing policies, material, production, styles, and workmanship. Every new process or idea that promises improvement is tried out. "Every shoe we sell evidences the wisdom and value of this policy."

A large mail-order house maintains a well-equipped laboratory for making both chemical and mechanical tests of the commodities which it handles. Since the policy of this house is to guarantee the goods to be as described in the catalogues it issues, sound business practice demands that the goods shall be tested as they come from the manufacturer. A special group of men are constantly busied in selecting commodities in stock, samples of which are sent to the laboratory for testing. If all-wool cloth is ordered from the manufacturer, this cloth is mechanically tested. Canned and preserved foods are tested chemically.

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[2] An advertisement.

Tests and analyses will, then, be made from various points of view, depending largely upon the function performed and the immediate or special interest. A pamphlet recently issued by the Silk Association of America urges one in buying clothes to "look to the seam." "Your only protection against extravagant cheapness and disappointment is to ask always before you buy: 'Is it sewed with silk?'" The ultimate distinction and durability, the Association claims, depend upon the seams being sewed with silk. On the other hand, the silk thread itself has its essential tests as illustrated by the following:

### OFFICIAL TESTS SILK VS. COTTON

(Made by the United States Conditioning and Testing Company)

*Test No. 1.* This test of the tensile or breaking strength of sewing silk and sewing cotton of the same size was made by the United States Conditioning and Testing Company. White Silk, Size A, proved to be 47 per cent stronger than white mercerized cotton equal in size.

*Test No. 2.* Made by the United States Conditioning and Testing Company. Black Silk Machine Twist and Black Mercerized Cotton equal in size were tested for elasticity. The silk proved to be more than three times as elastic as the cotton thread.

*Test No. 3.* This test of the tensile or breaking strength of silk and cotton seams was made. A strong inelastic cloth was sewed with white silk, size A, and a second piece was sewed with white cotton equal in size, both threads having the same yardage per ounce. Then each sample was subjected to a tension test. The silk seams were stronger than the material, while the cotton seams broke.

*Test No. 4.* In the sample sewed with silk the cloth itself ripped before the silk stitches of the seam gave way, but before the material broke the silk seam had withstood a strain 82 per cent greater than the strain under which the cotton thread had started to rip.

*Test No. 5.* Sample sewed with black silk, size B, was nearly four times stronger than a seam sewed with black cotton equal in size.

From the point of view of specific uses a commodity may be analyzed, first, for the kind and quality of the raw material entering into its composition; second, for the degree of care with which the article has been made; and, third, for the absence in the finished product of any material or materials detrimental to its use. The Federal Government is the greatest consumer of paper in the country and makes the following three kinds of tests: "First, physical tests are made to determine the weight per ream. The quadrant paper scale is used for this purpose. To determine thickness of the sheet a micrometer having a gauge reading to 1-10,000 of an inch is utilized. To learn the bursting strength a Mullen strength tester is employed. To determine the tension or breaking strength a Schopper folding machine is brought into play. The second class of tests which the government makes is microscopical tests. By these, the kinds of fiber used and the relative amounts are determined. The third kind of test is a chemical test. This is made to ascertain the amount and the nature of the coloring matter used."[3]

**180. Character of Demand.**—A part of the analysis of a commodity from a commercial point of view is a study of certain characteristics of demand. The article may have only an anticipated or potential demand. In this case the problem is first to adjust the goods to a known active or potential human want. Civilization progresses through education and education is in part the development of new economic wants. This is a long, drawn-out process. A new song may spread over the country in a single season, but the popular song demand is already there. Attention has been called to the fact that it has required as much as twenty years to educate a man to put a telephone in his house; that Edison pointed out the possibilities of his newly-invented phonograph in business correspondence in 1890, but the demand for talking machines among business men did not develop substantially for almost twenty years; that the thermos bottle was introduced in 1907 by a carefully-planned educational campaign, but only six years later did a demand arise for it among workmen for carrying hot liquids in their dinner pails.[4]

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[3] Levin. *The Marketing of Wrapping Paper*, p. 57

Or there may be a demand already developed for a given commodity. The problem then becomes one of better adjustment, one of competition in price, quality, or service. It is said that American ingenuity enabled hot-water bottles of domestic make to gain headway in Great Britain by adding a ring in the bottom by which it could be hung up to dry. The mail-order houses have found that farmers will buy starch in three-pound instead of one-pound packages, coffee in three to five-pound packages, and crackers in ten-pound cartons.

A commodity may be overdeveloped for the demand, not only in the sense that it is made in too large amounts, but also in the sense that it is overdone in itself. Many styles of goods that hold up in such metropolitan centers as New York City would not sell in a small-town market. But even this statement needs qualification. Shoe manufacturers have found certain small-town retail shoe stores in the Southwest that carry only a stock of high-grade shoes, such as would usually be carried in a large market center. Community taste and purchasing power are the determining factors. Nevertheless, a commodity may be overlaunched, like a street-railway system built on the possible growth of the next fifty years.

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[4] MacMartin, "Planning an Advertising Campaign for a Manufacturer," Part I, p. 12.

The taste of a community, that is, its standard of living, may require certain commodities to maintain this standard. Even the law courts have declared that certain conveniences and comforts are to be considered essential in certain strata of society. But apart from this phase, there are the essentials of modern life generally comprehended in the term "a reasonable minimum standard of living." These things have to do with food, shelter, clothing, fuel, light, heat, and various sundries. This class of goods may be called necessities. The problem of marketing them is fairly distinct.

Over and beyond the necessities stretches the range of luxuries. These are the extras of living. The line between the two groups is a shadowy one but the two fields in general are distinct. Again, it is largely a matter of taste and purchasing power. The same commodity, however, may be in one case a necessity and in another case a luxury. An automobile may be used as a delivery wagon or a touring car. A farmer may haul wheat to the local market in his automobile or take his family for a ride.

Furthermore, commodities are constantly passing from the luxury group to the necessity group. This is economic progress. Formerly furniture was built strictly for utility purposes; to-day it has a large style element in it. As civilization advances, it is hard to distinguish between the luxury of yesterday and the necessity of to-day. The telephone was once a great luxury, even in a business establishment; so also the typewriter. A camera may occasionally be used in scientific researches and experimentation, but on the whole it will be classified as a luxury. A commodity may work its way into the fiber of a living standard and be transferred from the status of a luxury to that of a necessity.

The demand may be either continuous or seasonal. In general, style goods are seasonal. There are hats for spring, summer, autumn, and winter. The demand for cameras is larger in the open-air seasons. Text books are in demand when the schools are in session, and especially at the beginning of the term. The commodities making up the large bulk of goods passing through the market have individual problems of their own. Consumption of bread varies with the weather, daily as well as seasonally. More baking, for example, is done in the family kitchen in the autumn and winter than in the spring and summer. The large bakeries have men skilled to estimate what these changes in demand will be. Retail stores will take advantage of sudden changes in weather to advertise rubbers or umbrellas or raincoats. The ups and downs of demand, for whatever cause, are a part of the commodity analysis.

A given commodity may serve directly to satisfy a human want, or may be used in conjunction with other commodities. The business of making automobile accessories may be called a contingent business, because the demand for its products is gauged by the demand for automobiles. Subsidiary industries, in the sense of contingent, or dependent, industries, are once removed from direct contact with the market. Just as the market for stocks and bonds is contingent upon the capital that is free for such investment, so the demand for dependent products varies with the demand for the primary product. A study of the demand for a commodity verges constantly into a study of the market. Nevertheless, a complete analysis of a product includes an understanding of all the peculiarities and fluctuations of the demand. All of these things affect the marketing problem.

**181. Supply of Commodity.**—The supply of a finished product may, in normal times, be controlled by the policy of the house. Every up-to-date mercantile establishment has its purchasing plan in the same way that a manufacturer has his purchasing plan. The formulation of this plan is a part of commodity analysis.

The purchasing problem is sometimes relatively simple. but often is very complex. A specialty store has practically a single line of goods to keep in stock. The retail grocer has hundreds, the druggist has thousands of articles to handle. A large hardware jobber carries 82,000 different articles. New lines have been added from time to time to the original shelf hardware upon which his business was founded, so as to include harness, paints, fencing, refrigerators, washing machines, sporting goods, cheap jewelry, automobile accessories, and so on.

The large mail-order houses must keep enough stock on their shelves to meet without delay the orders from their thousands upon thousands of customers. Managers of the various departments in these catalogue houses must in some way anticipate the demand for each kind of commodity under their control. When the order is in, it is then too late to make out the stock plan.

Whether simple or complex, the stock plan, to be made scientifically, requires a careful analysis of commodities. A manufacturer of rivets, screws, and other small linkage parts has studied so carefully the various classes of his commodities in relation to the demand for them, that he can prejudge to a nicety how many of each type to make. The retailer of shoes can adjust his sizes, styles, and qualities by systematic study to a seasonal demand. The buyer for a clothing manufacturer will estimate, as the time for "laying out" the spring or fall line arrives, the probable expenditure necessary, say, for woolens in each line. "From his knowledge of the various costs in the manufacture of a garment, he estimates that for his \$14.50 suit line he can afford woolens at \$1.00 per yard, for his \$17.50 line, woolens at \$1.12½. Thus, he figures that he will require 500 bolts of cloth priced at \$1.00—\$1.12½ a yard; 750 bolts of cloth at \$1.12½—\$1.25 a yard. In addition he attempts to anticipate the popular styles in woolens for the coming season. He knows the class of patterns desirable for his trade. He knows in a general way the styles emanating from London."

With such knowledge as this, the purchasing agent will go to the great Eastern markets. New York City is the center of the mill offices, and likewise contains magnificent sample rooms. These samples the purchasing agent examines for quality, weight, elasticity, hardness, cotton mixtures. Coarseness, elasticity, and mixture of cotton can be determined by the "feel" of the goods. A sure test of cloth fibers is to burn them. Slow burning and failure of the residue to disappear signify much cotton. Such a process in selecting quality and styles is analysis of a most direct and practical kind. A broad, detailed knowledge is essential for intelligent buying.

The qualifications of the purchasing agent include the following: (1) a knowledge of supply, sources always available, reliability of sources, quantities produced, possible substitutes; (2) a thorough knowledge of materials, *i.e.*, a detailed specification of all kinds, an expert knowledge of all grades, laboratory or other tests, simplest dependable methods of ascertaining qualities, and how goods stand up under wear; (3) a knowledge of prices, by kinds, qualities, grades, etc., past and present, and tendencies, seasonal variations, dominant price factors, discounts. This is only another way of saying that the purchasing agent must know the goods which he buys.

A most difficult problem is to evaluate the qualities of goods purchased. Is style or utility the important factor? The following is an attempt to weight the essential qualities or different grades of women's ready-to-wear garments:[5]

## Women's Ready-To-Wear

### *Inexpensive Grades*

| | | |
|---|---|---|
| 1. | Decision on price and delivery | 40% |
| 2. | Selection of styles, colors, and sizes | 30% |
| 3. | Determination of qualities, workmanship, finish | 20% |
| 4. | Arrangement of terms and discounts | 10% |

### *Medium Priced Grades*

| | | |
|---|---|---|
| 1. | Determination of qualities, workmanship, finish | 35% |
| 2. | Selection of styles, colors, and sizes | 30% |
| 3. | Decision on prices and deliveries | 20% |
| 4. | Arrangement of terms and discounts | 15% |

### *High Grades*

| | | |
|---|---|---|
| 1. | Selection of styles, colors, and sizes | 35% |
| 2. | Determination of qualities, workmanship, finish | 30% |
| 3. | Decision on prices and deliveries | 20% |
| 4. | Arrangement of terms and discounts | 15% |

One will not be deceived by the specific character of these percentages, but the relative importance of the various considerations is of value. On inexpensive goods, price is of prime importance, but recedes to third place in higher grades. Styles have a subordinate place in buying inexpensive grades; in buying high grades, it is the first consideration. It is to be noted further that "terms and discounts" are considered last in all grades.

A further example of the practical analysis of goods may be taken from the same source:[6]

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[5] Field, *Retail Buying*, p. 55.

[6] *Ibid.*, p. 56.

### MEDIUM PRICED READY-TO-WEAR MERCHANDISE

1. Determination of qualities, workmanship, and finish:

| | | |
|---|---|---|
| a. | Testing for raw material | 6% |
| b. | Judging process of manufacture | 3% |
| c. | Estimating cost of manufacture | 4% |
| d. | Feeling for weight | 2% |
| e. | Sizing up any guarantee | 6% |
| f. | Examining for flaws | 5% |
| g. | Valuing the finish (machine or hand) | 4% |
| h. | Ascertaining care used in exterior finish | 2% |
| i. | Ascertaining care used in interior finish | 3% |
| | Total | 35% |

Once again the definite figure is of less importance than the relative value. It is interesting to note that the guarantee is considered the most important single factor in the analysis of qualities, workmanship, and finish. The reason doubtless is that a guarantee may lighten the risks of judgment on all the items. This practical judgment of goods is the application of principles of analysis to them. Sooner or later the characteristics of a commodity must be evaluated in reference to demand and price. Part of this task falls upon the purchasing agent. The salesman attempts to realize on the purchasing agent's judgment.

**182. Analysis a Middleman Function.**—The analysis of finished goods, especially relative to market demand and price, is the function of the merchant. The manufacturer seeks through a careful analysis of materials and by standardized processes to turn out a product true in every respect to a preconceived pattern. It is the task of the merchant to know how such commodities will satisfy human wants. To the druggist is left the job of filling a prescription; the retail merchant may be handling commodities equally important to health and comfort. The druggist is presumed to be trained and to be equipped with a laboratory for his work; the retailer needs to rise to the same level.

There is no reason why retail stores should not be equipped with laboratories and manned by clerks who have some claim to being experts. In some kinds of retail business a laboratory may become as important as the refrigerator. In that case there will be less need for a pure food and drug act. Wholesalers are already realizing the value of careful scientific analysis of the commodities they handle.

The middleman, however, is likely to classify his goods on the most convenient basis. The distinction into classes of agricultural commodities has been made as follows: harvesting machinery, tillage implements, threshing outfits, and side lines. The reason for this is largely one of origin and emphasis, but has to do also with phases of demand. Another classification of commodities, along the lines of principles determining the location of retail stores and types of distributive systems, is: emergency goods, convenience goods, and shopping lines. Groceries have been divided into staples, fancies, and specialties. Automobiles are classified (1) on the basis of motive power into gasoline, steam, and electric; (2) on the basis of price as (*a*) $5,000 and over, or high-grade car, (*b*) the $2,000, or medium grade car, (*c*) the $1,000 car and (*d*) the Ford. Every step toward classification is, however, a step toward analysis. The more carefully it is done, the more thoroughly it is done, the more intelligent will be the business methods.

**183. Analysis and Grading.**—It is to be noted in this connection that the process of commodity analysis is a process of establishing standard grades. For grades to be scientifically determined, they must be founded upon the want-satisfying qualities or the utility of the goods.

Classification and grading must be for a purpose. In merchandising, the purpose is most effectively to match commodities against wants. Therefore, just as raw materials are analyzed to construct from them a predesigned product, so finished goods are analyzed to isolate and identify their utilities. The basis of all scientific grading is value in the economic sense. For example, oranges have been analyzed for their relative food value, that is, the amount of calories which they contain as compared with oysters, buttermilk, and so forth,[7] their use as a food in fever cases, as a substitute for water, and the "vitamines" which they contain; cloth is tested for shrinkage; typewriters for durability, speed, adaptability, convenience, ease of operation, ease and cheapness of keeping in repair; an automobile as to service or style.

**184. Analysis and the Market.**—Goods are made and goods are handled to satisfy human wants. The sum total of human wants is the possible market for products. Into every consideration of every commodity, therefore, enters the element of demand. In fact, goods cannot be analyzed apart from the market. There is, therefore, a vital interrelation between the market and the product. It is not logical to attempt to analyze a commodity simply as a thing in itself, because it is desirable only in so far as it is useful.

## SUGGESTIONS FOR STUDY

The student should continue his study of a specific commodity in connection with the problems of this chapter. It would be wise to select a finished product into which the raw material of the preceding section has entered. The following points will serve as topics for classroom discussion:

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[7] Bulletin No. 28, U. S. Department of Agriculture.

1. The educational value of analysis.
2. The style element as a commercial factor.
3. Sources of data for a stock plan.
4. Qualifications of a purchasing agent.
5. Analysis and turnover of stock.
6. Bargain sales and commodity analysis.
7. Natural sciences and commodity analysis.
8. Utility analysis.
9. Evaluating qualities in terms of price.
10. "Humanizing" commodities.

READINGS:

MacMartin, "Planning an Advertising Campaign for a Manufacturer," Part I.
Shaw, *Approach to Business Problems,* Chap. X.
Ivey, *Essentials of Retail Salesmanship,* Chaps. III, IV.
Field, *Retail Buying,* Chaps. IV, VI.
Nystrom, *Economics of Retailing,* Chap. XVII.
——*Retail Store Management,* Chaps. III, V.
Terry, *How to Keep a Store,* Chap. IV.

# CHAPTER XIV

## ANALYZING THE MARKET

**185. Some Aspects of Market Analysis.**—The market in its broadest sense, we have said, means demand, or in economic phraseology, effective demand—a demand with the compelling force of purchasing power behind it. In this sense the term is used here, because it holds equally true for finished goods. A market is a chance to buy or sell. The merchant is ever on the lookout for a chance to buy or to sell, at a profit to himself. His great problem is demand creation; he must seek out his own market in the midst of keen competition. As has been pointed out, the merchant must buy with skill and judgment, but this skill and judgment will be derived largely from a thorough knowledge of the market. In these modern days it is necessary for the merchant to study his market in advance.

What this market is in broad outlines, what factors enter into it, what changes occur, what development there has been, how to estimate it—in a word, how to study it in advance—is the problem of this chapter. An attempt will be made to outline the principles by means of which the market may be analyzed. Much will depend upon the point of view from which the problem is approached. In general terms a market may be analyzed on the basis of (1) the character of the commodity, (2) the grades of commodities, (3) prices of commodities; or from the reverse angle, on the basis of (1) the character of the population, (2) the number of people in the market area, (3) the purchasing power and its distribution, (4) buying habits,

(5) standards of living, (6) occupations, and (7) climatic conditions. In one case, the line of vision is from the individual toward the commodity; in the other case, it is from the commodity toward the individual.

**186. Trade Geography.**—Politically, men think in terms of certain clearly defined divisions, whether federal, state, or local. Tariff walls attempt to apply political delimitations to markets. The United States Census is founded on political units, for industry and commerce as well as for ethnology and agriculture. So common is the custom of using political units, that the idea tends to be accepted that these are natural divisions of the country. As a matter of fact they are not natural divisions from any point of view, and especially is this true of trade. Market boundaries do not follow state or local political boundaries at all. They do not coincide with the larger divisions made by the Interstate Commerce Commission for the classification of freight. In other words, commercial sections are not politically or physically distinct sections. Market areas overlap almost promiscuously. A geography of the United States made on the basis of retail-market conditions would be a striking one.

If one will look at the country from the point of view of trade, he will find three fairly distinct divisions. One is the city market, another is the suburban market, and a third is the country market. It is not possible, of course, to make a clear-cut division, but the distinction will serve as a practical one. There are many rapid changes occurring to-day which tend to make the lines of division more shadowy, such as good roads. automobiles, and a redistribution of purchasing power.

The city trade will fall into two general classes. One of these may be called the metropolitan market; the other, the general city market. The metropolitan market may be outlined by drawing a line from Portland, Maine, so as to include Massachusetts, Connecticut, and part of New York and Pennsylvania, ending somewhere below Wilmington, Delaware. This is the greatest retail section of the United States. It contains three of the largest and wealthiest cities, New York, Philadelphia, and Boston. It marks off also the region of concentrated manufacturing and of wealth. The dominating factors emanate from the three great centers named.

The general city trade is made up of the trading centers throughout the United States ranging from 60,000 or 75,000 inhabitants up to one million or more. These centers in all parts of the country outside of the metropolitan region have certain characteristics in common. The suburban market consists of smaller towns, which are satellites to the larger ones. Cities of 75,000 or below may be called suburban. The country trade is made up of the rural districts proper and small towns having up to 2,500 inhabitants.

In the trade geography for textiles, for example, the important point to keep in mind is that these goods fall into three classes. There are the shopping lines, the emergency-goods lines, and the convenience-goods lines. The metropolitan market is the great shopping center. For this reason the textile buyers have flocked to the Eastern trade centers to do their buying, because they found there the best shopping opportunities. These shopping opportunities depend, of course, upon the fact that it is possible to compare so many different lines. The metropolitan market reaches out to dominate the shopping trade. This creates a problem for the general city and the suburban market, where the dealers must struggle for a share of the shopping trade. The main bulk of their sales, however, will be in emergency and convenience goods. The country store will struggle in its turn with the larger trade center for a meager share of the shopping trade, but will depend in its turn also in the main upon emergency and convenience goods.

Geographical divisions will have to be varied for other commodities than textiles, but in general these are basic in the finished-goods trade. St. Louis is a dominating figure in shelf hardware, with Chicago a close second. The latter towers up in canned goods and railway supplies. Minneapolis is important in the flour trade. The point is that a great trade center tends to control the lines of trade. Boston practically dominates the New England market and typifies the Yankee buying habits. The region dominated by New York City is the great spending center of the country. There may be found the most expensive displays in the United States. The New York market runs on the basis of style with price a subordinate factor, as contrasted with the careful Yankee shopper. The outstanding attributes of the Middle West are frugality, stability, and conservatism, applying both to styles and prices, and emphasizing utility. Thus, Chicago sells an enormous volume of staples and is, without doubt, the greatest jobbing center for general merchandise, as well as for textiles. It is significant, too, that Chicago has the largest retail stores in the country and the greatest mail-order houses in the world.

The geographical lines of trade are shifting and irregular, because the elements upon which they are founded are so. Among these elements the following are to be considered; means of travel, nationality, purchasing power, buying habits, and many psychological influences. It is very much worth while, however, to ascertain as definitely as possible these regions.

**187. Historical Considerations.**—To get a proper perspective of market conditions, it is necessary to trace their development. The development of demand is economic progress. In order to understand present conditions and to determine future tendencies one should make an historical survey of the market. There is a mine of valuable information, for example, in the mail-order catalogs put out by the leading houses. It would be possible to write the history of trade in many lines of merchandise by a study of those catalogs, running back to 1874. What new kinds of goods have appeared, how they have held up, how they have changed, why certain ones have disappeared, why they have reappeared, and how the quality has been toned up, could be learned by such an investigation. At the same time, one would become versed in market psychology.

What could be done in this way for the country market could be done for other markets by other means. Advertisements in newspapers, in magazines, on billboards, and elsewhere can be studied progressively. An individual business affords the opportunity for the same kind of study. What the market has taken and what the market has refused to take are both of significance.

Progress in demand can be made in two general ways. One is by the development of new wants; the other by an intensifying, or elaboration, of existing wants. There was first a demand for a horseless carriage, and the driver of it was willing to endure the jiggling and jolting, the noise of the engine, and the difficulty of starting it. From this crude beginning there has developed the luxurious car of to-day with all of its conveniences and accessories. This example is typical of market progress; first a demand, however stimulated, then a gradual refinement of it. The telephone was in the beginning a luxury even in business, but to-day is a necessity in business and in most homes. Besides, there have developed numerous conveniences to facilitate the use of it.

Other important facts will be learned from a study of market development. There are the changes in taste, in the level of the standard of living. There is the long groundswell of market fluctuation to be compared and contrasted with the short, choppy ones. Furthermore, markets never stand still; they are dynamic, not static. It is of great importance, therefore, to determine as accurately as possible how the markets are moving, whether toward an increase or toward a decrease, and why. The same kinds of advantages accrue from an historical knowledge of the market as from an historical knowledge of the political situation. If one can know where we are and whither we are tending, one can better know what to do and how to do it, in trade as well as in politics. Merchants will do themselves a great service by keeping records in such a way as to make possible a survey of business development.

**188. Market Units.**—Ultimately, the unit reached in market analysis is the individual. He is the consumer. Of his importance one business investigator has written: "The manufacturer should never lose sight of the fact that *over all this army of middlemen, the consumer is king.* What he demands, they buy—what he refuses, they reject; and King Consumer demands and refuses on the basis of quality. His whim makes and unmakes manufacturer, jobber, and retailer. Whoever wins his confidence has won the market; whoever loses it is lost."[1]

Of these individual consumers there are in the United States about 105,000,000. This is a vast market to which to appeal. But the rewards of successful appeal are so tremendous as to stimulate repeated attempts. The individual market itself is constantly shifting and changing. To know it thoroughly is to know these millions of individualities. This problem has too many variables for solution. There are, in fact, other ways to approach it than through the individual unit.

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[1] Address by C. C. Parlin.

The most common buying unit in the market is the family. This offers a composite demand through a single buying medium, usually the woman in the household as a purchasing agent. It has been estimated that women make about 75 per cent of the household purchases. A large part, therefore, of the appeals to consumers can be made to them. Sex becomes a prominent consideration in market analysis.

The market unit, however, will be influenced by several considerations. There is, first, the kind of commodity. No one would think of planning a sales campaign for steam excavators on the family unit basis, or cash registers, or comptometers. In this connection, it is necessary to distinguish between those goods which minister directly to human wants, usually known as consumers' goods, and those used to produce them, or producers' goods. The latter will run on a different market unit than the former. In fact, the individual and the family units are usually applied to consumers' goods. Producers' goods may be based upon an individual establishment, an industry, or a community. A railway terminal, a road, a public building, are judged on a broad community unit.

The character of population will also influence the market unit. There are individualistic qualities and clannish qualities; there are religious regulations and social requirements; there are purchasing power, prices, and grades of commodities also to be considered; there are occupations and ages as factors. The analysis, even from this point of view, is never complete.

**189. Social Elements in the Market.**—Whatever the commodity and whatever the unit considered, a prime factor in understanding the market is to know the fundamental social elements. In general, the social study of mankind divides itself into two parts; one has to do with physical phenomena, the other with mental. Bodily form and activities are physical in character and offer an opportunity to study society from the point of view of physical energy. The physical facts to be considered in this respect are: (1) birth rates, (2) migration, (3) groupings, (4) employment, and (5) sex. Back of these there are some elementary physical laws which may be stated broadly as follows: (*a*) there is a balance, or equilbrium, of forces between a population and its environment, *i.e.*, "all energy expended in the growth and activity of a population is derived from the physical world," thus determining the virility and density of population; (*b*) as a corollary it follows that, given a population, and other things being equal, "social activity varies with the harvests," showing a correlation between good or bad times and the marriage, birth, and death rate; (*c*) social activity follows the line of least resistance, in migrating, in concentrating, in determining occupations.

Of the mental phenomena, the most important are the group characteristics. Fundamental here is the "law of least effort." It is a human desire to attain satisfaction with a minimum of difficulty. There is an interest and a pleasure in finding a likeness between oneself and others. A further characteristic is a response or lack of response to the same stimuli; the former is sympathy, the latter antipathy or prejudice. In any group, also, there is a desire for a diversity of satisfaction, always extending in one way or another the marginal utility.

In the market, as in other phases of social activity, there are leaders. Strong personality, superior mental vigor, aggressiveness, are important in determining the direction of demand. There are leaders in every market for every kind of commodity; there are leaders in buying thought just as there are leaders in political and religious thought. The merchant, and especially the retail merchant, should try to identify and appeal to these leaders in the market.

If the consumer is king, these leaders are kings of kings. If the consumer thinks for the retailer, these leaders think for the mass of consumers.

Leadership in demand depends largely upon the powerful force of imitation. People imitate those whom they admire or respect. Those who are admired may be neighbors or strangers; natives or foreigners; real persons or fictitious characters. Every "best seller," through illustrations and descriptions, has a market influence. Actors and actresses exert a powerful influence. The power of movie stars in this respect is very well recognized. Certain illustrators have developed types, both of men and women, that receive wide imitation.

Through the power of leadership and by imitation, in general, buying habits are developed. There come to be within the broader market certain commodity areas. In certain districts the farmers will use only a left-handed plow; in others a right-handed plow is preferred. In some sections a wide-tired wagon is most popular; in others, and without justifiable reasons, a narrow tire. In Boston, for example, a most familiar sight is a peculiarly shaped double-handled handbag. This bag has made inroads into the field preëmpted in old times by the Harvard green bag. There are, also, corn-bread areas and sauerkraut areas. Wherever there is stability in a community these buying habits tend to develop. In some parts of the country to-day, however, the consumers' map represents an intricate and shifting problem. Because the market is made up of people, individuals and groups, the problem of analysis is permeated by social considerations. Mass psychology becomes important for the merchant in analyzing his market.

**190. Population Movements.**—A market is made up of people, and therefore changes as the people change. A new generation may mark a radical departure in buying habits. But in a comparatively new and rapidly developing country it is even more important to trace the ebb and flow of people. Certain districts in Chicago were greatly changed within a single year by the influx of more than 10,000 negroes from the South. Within the lifetime of a single individual a New England town has changed its racial characteristics three or four times. The older type of New Englander gave place to the Irish immigrant; the Irishman, in his turn, yielded to the French-Canadian, who was supplanted by the Italian. Since the coming of Italians there has been a dilution from half a dozen different sources. The market has been kaleidoscopic.

The census reports have shown, from period to period, the results of population movements. The one now being taken will likewise reveal some interesting facts. Wholesaler and retailer should watch for them. Racial characteristics are clearly marked in buying habits. In a certain town in Missouri one part is occupied by people who came from Ohio, Illinois, and Indiana; the other part is occupied by Southerners. An open city market was successful in the former section, but a failure in the latter.

**191. Population Analysis.**—The same plan of population analysis may be applied generally. Some of the most important considerations are:

1. *Age Distribution.*—Usually the parents decide upon purchases, but in the United States a growing influence of children is noted. This has led to an appeal to the children in an attempt, through them, to direct purchasing power.

2. *Sex.*—Not only is the demand different for different sexes, but also the method of appeal must differ. In general, women are more careful buyers than men. Some psychological tests were recently made with the following deductions: (*a*) women buy men's goods eleven times as much as men buy women's goods; (*b*) women help men buy twice as much as men help women buy; (*c*) men only

help to buy advertised goods; (*d*) women alone purchase 48.4 per cent. of all goods; adding what both buy together equals 59.9 per cent.; (*e*) women respond more quickly to appeals to their dislikes, men to appeals to preferences; (*f*) the problem with men is to get attention, with women, to hold it; (*g*) women invariably respond more quickly to an eye appeal (pictures) than men, who usually prefer reading matter; (*h*) women are less apt to take up with something new; (*i*) women respond most quickly to personal appeals, men to appeals of a social sort. These psychological guesses indicate the significance of sex in population analysis.

3. *Habits.*—These may be social, racial, or personal, but in so far as they affect method and quantity of buying they are important for market analysis.

4. *Occupations.*—The same kind of work makes a bond between men. Printers, carpenters, miners, and so on, have some things in common, however much they may differ in certain qualities.

5. *Living Conditions.*—Men of certain ranges of purchasing power tend to adopt similar standards of living, but, of course, the city dweller of the same economic status will have different demands from the suburban or country man. A recent survey of families with incomes ranging from $2,000 to $5,000 per year showed that 72 per cent lived in apartments and 60 per cent had neither vehicles nor musical instruments. Another survey used the amount of rent paid as a criterion of economic status. Some groups, for example, in university neighborhoods, have tastes developed regardless of economic status.

6. *Purchasing Power.*—Men cannot buy without purchasing power. It would be useless to try to market high-priced limousines in the hill counties of Arkansas. A demand might be found but it would not be an effective demand.

7. *Climatic Considerations.*—Obviously, wants are modified by climatic conditions. Economic progress is led and directed from the temperate zone. Apart from the physical and mental stimulus of a vigorous climate, there is the very practical consideration of food, shelter, and clothing. Within our own country, also, there are significant differences. The population on the plains is one problem; dwellers among the hills and mountains are another. Climate among many other things distinguishes the South from the North, the East from the West, New England from California, Texas from Minnesota.

8. *Social Strata.*—Society tends to divide itself into strata along several different lines: one is wealth; another is education; a third, racial; a fourth, religious; a fifth, ancestral. All of these things affect the marketing problem.

**192. Incomes.**—In connection with the question of purchasing power within the market comes another having to do with the distribution of it. How much expenditure can there be per unit, whether the unit is the individual, the family, or the community? It was estimated from the last census data that 27 per cent of the total aggregate income in the United States goes to the poorer half of the families and 73 per cent to the richer half; that 10 per cent of the families gets from three-fifths to two-thirds of the total income. Even here it is required to descend to those receiving between $1,200 and $1,800 to make up the 10 per cent. No doubt the figures are to-day much changed. This redistribution of wealth is a great new factor in market analysis.

It is not the amount of money that the income represents, but the buying power of that money that counts in the market. Just as there is a real and a nominal wage, so there is a real and a nominal income. An income has its true significance in relation to prices, and the income must be judged on a unit basis—as individual, family, or community. No one has an "average" income to spend. It is necessary to consider the distribution of incomes. The market responds most quickly to a well proportioned range of income; not necessarily an equal, but a widespread, generous income.

**193. Budgets.**—Typical, representative, or average budgets have often been constructed to show how the income is spent. This has been done both for the individual, that is, for the single man and the single woman, and for the typical American family consisting of the two parents and three children. The items have been calculated both absolutely and by percentages. A table giving the percentages of expenditures for various purposes is shown for 1914.

| Item | Per Cent of Total Income |
|---|---|
| Food | 43% |
| Shelter | 18% |
| Clothing | 13% |
| Fuel, heat, light | 6% |
| Sundries | 20% |

This specimen budget, obtained by the Bureau of Labor Statistics, is constructed from a broad survey. Although it may not fit precisely the expenditures of any one family, the general tendency is to approximate this. The local conditions behind any average budget should always be carefully considered. In one case rents will be high; in another, food, and so on.

It is essential to note in this connection that the relative importance of the budgetary items changes with changing prices. A given budget represents average conditions at the ruling prices. War prices made chaos of the prewar percentage budget. The relative importance of food has increased; shelter has fallen to about 8 per cent; clothing has gone up to nearly 20 per cent; fuel, heat, and light have decreased in importance; sundries are also less important. It is obvious that if an income remains fixed and some item in the budget rises, there must be a corresponding decrease elsewhere.

A budget, with estimated absolute amounts, was made by the Department of Labor, to represent the expenditure necessary to maintain a reasonable standard of living. As indicated, this budget is for a single man or a single woman.

Summary of Annual Budget

| Items | Man | Woman |
|---|---|---|
| 1. Room (2 in room) $15 per month per person | $180.00 | $180.00 |
| 2. Board: | | |
| Regular table board, 2 meals on weekdays, 3 on Sunday, $6 per week....... | 312.00 | 312.00 |
| Lunch, 25 cents per day for 313 days.... | 78.25 | 78.25 |
| Other food, confectionery, etc., 25 cents per week.......................... | 13.00 | 13.00 |
| 3. Clothing............................ | 158.36 | 240.15 |
| 4. Laundry............................. | 52.00 | 65.00 |
| 5. Toilet supplies..................... | 15.00 | 10.00 |
| 6. Health, medicine, dentist, oculist........ | 32.00 | 43.00 |
| 7. Religious organization................. | 5.20 | 5.20 |
| 8. Labor organization.................... | 5.00 | 5.00 |
| 9. Newspapers.......................... | 8.40 | 8.40 |
| 10. Books and magazines.................. | ..... | ..... |
| 11. Carfare............................ | 37.20 | 37.20 |
| 12. Amusements......................... | 39.00 | 20.00 |
| 13. Vacations........................... | ..... | ..... |
| 14. Educational purposes................. | ..... | ..... |
| 15. Other incidentals..................... | 26.00 | 20.00 |
| | $961.41 | $1037.20 |
| 16. Savings 10%......................... | 96.14 | 103.72 |
| | $1057.55 | $1140.92 |

Such budgets are at least a vague indication of the drift of expenditure. It adds to one's knowledge of the market to learn, in addition to an estimate of income, that is, the total amount to be expended, something as to the relative division of expenditure. It was estimated several years ago that the consumption of food in the United States amounted to six and a half billion dollars. To-day the figure is much larger, because of a more widely-spread purchasing power, and because food prices have risen more than one hundred per cent over that period. The estimated amount spent for clothing in the United States was at that time about $2,178,400,000; for shoes, $520,000,000 per year; for furniture, about the same; for books and paper, about $166,400,000.[2]

**194. Individual Items.**—Many different calculations have been made as to the consumption in total amounts and per capita of various specific commodities. To the individual merchant the great concern is the actual and potential market for the product which he handles. It has been said that the consumption of sugar is about 85 pounds per capita. Furthermore, it is claimed that country people eat more sugar than city people. This estimate would make the total consumption in the United States about 405,000,000 pounds annually. A newspaper, with a circulation of 357,689, claimed that within the territory reached by it, there were used about 2,000,000 bottles of ammonia for washing and cleansing purposes alone, about 178,000 carpet sweepers, about 1,430,000 brooms, 357,000 mops, 9,942,000 packages of washing powder, about 89,000 wringers and 89,000 washing machines, together with 1,788,000 cakes of soap.

Certain clearly defined groups have certain clearly defined needs. There are probably 600 libraries that have a policy of buying every book of general interest that is published. This is typical of the market that can be "counted on." It has also been pointed out that there are approximately 25,000,000 public school children under compulsory gymnastic training; that there are 50,000,000 boys and girls, young men and young women, between the ages of 5 and 24, interested in outdoor and indoor games. For these groups and for this interest certain articles are needed.

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[2] *National Advertising, the Modern Selling Force,* p. 44.

Every commodity has, of course, its own market. Sometimes this market is definitely limited, by price, by the lasting qualities of the product, by the fact that demand cannot be expended, and so on. Furniture is not bought as frequently as shoes or clothing; an expensive automobile has a smaller potential market than a low-priced one; not as many fur coats as neckties can be sold to an individual. There are numberless influences in the market that need watching for their effect upon the demand for individual commodities. A wet summer will call for more lawn-mowers; a dry summer for more feet of rubber hose. "Steel traps for catching fur-bearings animals sell best when the price of skins is high." The announcement that flies carry disease germs boosted the market for "fly killers." The change in fashion from carpets to rugs cut down the market for carpet stretchers and tacks. The list of illustrations is interminable.

**195. Shifting Demand.**—Demand may change from a great variety of causes. It may be due to the caprice or whim of a fickle public taste. This applies especially to style goods. "Just what determines the selling properties of a design remains a mystery to the wisest dress-goods designer. Two designs may be identical except for some trifling difference in structure. One may be a good seller, while the other fails to move at all."[3]

The change may come with no well-defined cause behind it. However excellent a product may be, there may be a drift from it to a newer article. The American public is forever seeking some new thing. It has been said that the makers of breakfast foods found a shift from wheat to corn, which continued despite advertising.

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[3] Cherington, *The Wool Industry,* p. 179.

In the regular course of economic progress, there may come a change in demand for certain commodities. Better grades of clothing may be worn by a new generation. There may be better furniture, better houses; high-priced pianos may displace cheap organs. The new generation may find spending money "easy," and live in general on a higher standard.

Demand may shift suddenly through legislative enactment. This is illustrated by the Eighteenth Amendment to the Federal Constitution. It has been calculated that as much as $2,000,000,000 was spent annually for liquor in the United States. A great part of this sum has now been diverted to other purchases. Where has it gone? Increased purchases are reported of soft drinks, candy, and tobacco. Retailers of other goods say that they have noticed that more purchases are being made which they attribute to money saved from drink. Savings banks report increased deposits. Somewhere a vast sum has gone into purchases and hundreds of thousands of family budgets have been changed.

**196. Form and Scope of a Market.**—The scope of a market may be judged with more or less accuracy on a geographical basis. In this respect it will be modified by the character of the commodity itself. A wide market requires products that are in general demand, and that are small in bulk and light in weight as compared with their value. These products must also be durable. All of these requirements, however, are being modified by better marketing facilities. Nevertheless, under strongly competitive conditions, the location of producing plants in relation to the market will always be an important consideration.

The form of the market will be modified by accidental relations, such as chance acquaintance, or a strong advertisement coming at a strategic moment, and in countless other ways; by new facilities, such as railroads or steamship lines; by natural barriers, such as mountains or bodies of water; by artificial barriers, such as a tariff, hostility, prejudice. As a rule, trade follows the line of least resistance. Theoretically, a commercial area would be circular in shape, with the productive area at or near the center. No market is ever actually so. The commercial area dominated by Chicago is modified by the lakes and the Canadian boundary. It has been extended across the broad prairies of the Northwest and the West, but its power has been broken to some extent by the rise of other trade centers, Milwaukee, Minneapolis, Kansas City. There has been a long struggle with St. Louis on the southwest. Recently the market boundary was extended toward the southeast when a new opening for Chicago products was made along new railway lines that were finally able to break a way into Chicago.

**197. Financial and Trade Conditions.**—A powerful influence on market demand is found in the financial and trade conditions. A good basic crop on the farms, such as corn, wheat, or cotton, makes a tremendous difference in purchasing power. The large mail-order houses have experts in the field for the purpose of keeping in touch with crop conditions, so important do they consider this information. The southern market has been revolutionized by the high price of cotton.

The fundamental importance of financial conditions was fully demonstrated in the panic of 1907. The very lifeblood of trade was congealed. What a chaotic condition of foreign exchange can do has been demonstrated by the experience since the armistice. When money becomes "tight," when no credits are extended, the purchasing power of the market is prevented from activity; demand is only potentially effective. It may be noted, however, that a panic does not close the avenues to market. A corn syrup was launched as a new product in the midst of a panic and achieved "immediate success because people welcomed a spread for bread that was cheaper than butter and jam."[4]

**198. The Human Element.**—It cannot be emphasized too strongly that a study of the market for manufactured goods is a study of people. Retailer and wholesaler and manufacturer are primarily interested in people; for them the consumer is an "economic man." What people think economically, how they are pecuniarily motivated, how they may be appealed to, what their defenses are—these things form a large part of the subject matter of market analysis.

The study of people, even as mere consumers, is an infinitely varying and a perennially interesting one. It offers full play for all one's faculties. The power of careful observation, of accurate recording of impressions, of discovering motives and reactions, of imagination, of knowing, in brief, the human mind and heart, is an inestimable asset in market analysis. "A man is a bundle of relations, a knot of roots, whose flower and fruitage is the world." The market is as interesting and as complex as human nature.

## SUGGESTIONS FOR STUDY

The market for the commodity selected for study should be analyzed at this point. The following problems will serve for class discussion:

1. Take the definition of the market as "a chance to sell at a profit," and try to formulate some guiding principles for investigation.

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[4] MacMartin, "Planning an Advertising Campaign for a Manufacturer," Part II, p. 68.

2. Suppose a manufacturer in Chicago asks you for information on the market possibilities of his product, say bicycles, in the Piedmont District of North Carolina. How would you begin?
3. Consumption balanced against "square mileage." Discuss.
4. What, in your judgment, would be sound criteria for determining (*a*) standards of living, (*b*) purchasing power, (*c*) "likes and dislikes," in any given market area?
5. Relate the whole problem of market analysis to the "guidance of economic activity."
6. What physical condition in the commercial area needs to be studied?
7. What is the most valuable unit, and why, upon which to base a population analysis? (*a*) Social group. (*b*) Family. (*c*) Individual.
8. A sales manager speaks of "factors of resistance" in a certain territory. What can he mean?
9. Criticize the use of a family budget as a basis for judging market demand.
10. "Consumer is King." Discuss.

READINGS:

Shaw, *Some Problems in Market Distribution,* Chaps. II, IV; *An Approach to Business Problems,* Chap. XIV.

Cherington, *Advertising as a Business Force,* Chaps. I, V.

Fisk, *Retail Selling,* Chaps. I, II.

MacMartin, "Planning an Advertising Campaign for a Manufacturer," Part II.

Giddings, *Elements of Sociology,* Chap. XII.

*Printers' Ink,* September, 25, 1913, p. 17; July 31, 1913, p. 17; December 31, 1914, p. 74; October 30, 1913, p. 19; March 12, 1915, p. 37.

*System,* February, 1913, p. 115; May, 1916, p. 451.

# CHAPTER XV

## THE DISTRIBUTIVE ORGANIZATION

The name given to the mechanism for distributing goods, both geographically and in point of time, as they are needed, is the distributive organization. It is the function of this organization to create time and place utilities, and those middlemen who are engaged in such activity are presumably rewarded commensurate with the service thus performed.

**199. Character of Distributive Organization.**—The distributive organization of to-day is not of sudden growth, nor has it yet ceased to change and develop. All types of business organization have come into being in response to an economic need; they tend to fall into decay and to disappear when the need is gone. They live and thrive by service. With the widening of markets and the specialization of functions, the distributive organization has at first grown in magnitude and in complexity, and then tended to become simpler and more direct under the influence of standardization and identification of commodities, and of advertising.

Parts of the trade organization, however, have tended to crystallize, or fossilize, and to persist after their usefulness is gone. This is a common experience with individuals and groups. The old dog cannot learn new tricks. Old machinery in the shop is retained often long after it has ceased to be efficient. Old methods of production have continued in spite of new inventions and better methods. The spinning wheel, the hand loom, the flail, the water wheel, have not wholly vanished from the earth. In the distribution of goods, also, old methods and outworn processes have not been altogether cleared away. Caught in an eddy of unprogressiveness, they have escaped destruction. Nevertheless, it is true, in general, that in the slow processes of time useless parts are worn away.

The distributive organization is made up of institutions and functions. "An institution consists of a concept (idea, notion, doctrine, interest) and a structure. The structure is a framework or apparatus, set to coöperate in prescribed ways at a certain conjuncture. The structure holds the concept and furnishes instrumentalities for bringing it into the world of facts and action in a way to serve the interests of men in society."[1]

That is, there are certain types of organization or certain institutions through which men work to accomplish a desired end. The process of distributing goods is the process of men working through certain mechanisms and devices which they have developed and which make their work most effective. The purposes in view are the functions. The machinery and the devices are the institutions. Distribution, like production, has its machinery.

The primary purpose of the distributive organization is obviously to carry goods from the manufacturer to the consumer. In order to do this task effectively, there is needed a thorough knowledge of the commodity itself, and of its market. This means that market information is essential for the effective direction and for the economic adjustment of supply and demand. It is the duty of the middlemen who work through the distributive organization to satisfy established wants and to develop new wants. It is also their duty to distribute goods both geographically and in point of time as they are needed.

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[1] Sumner, *Folkways*, p. 53.

It is this distributive machinery, constructed for these purposes, that is to be analyzed in this discussion. How it has developed, the character and function of its various parts, its operation to-day, and the tendencies toward modification for future services will be discussed. The trade organization for handling raw materials and foodstuffs was analyzed from the point of view of definite functions. The distributive organization designed to handle manufactured goods will be examined from a new angle. In the case of raw materials and foodstuffs, attention was centered on the control of commodities and the risks undertaken. In the case of manufactured goods, emphasis will be upon the attempt by producer, wholesaler, and retailer to control and direct the consumer demand for his own benefit.

**200. Development of Distributive Organization.**—Commercially and industrially, as well as politically, the beginnings on this continent were British in character. The manufacture of goods by the colonists was forbidden by law, and the importation from non-British sources was restricted. The distributive problem, therefore, as connected with manufactured goods, was very largely one for the importer. British goods were brought to the ports along the Atlantic seaboard, entered in the storehouses there, and were carried thence to the colonists up and down the coast and along the river courses. The sea and the rivers offered at first the only open highways of traffic; inland was the trackless wilderness.

It was necessary for the early settlers to adjust themselves to a pioneer environment; they were forced to provide food, shelter, and clothing. The need of tools and household utensils was imperative. Household manufacture, therefore, could not be wholly suppressed. It was not a primitive people who settled this country, but men and women skilled in the arts and crafts of that day, and with a background of knowledge and experience with an advanced civilization. They were familiar with household manufacturing, with roads, canals, conveyances, ships, banks, money, wholesaling, and retailing.

Marketing methods, therefore, in this country were transplanted from Europe, and were adjusted to the pioneer conditions, although largely controlled by restrictive laws. With the rise of a spirit of independence, domestic manufacturing quickened. Iron ore was secured from swamp deposits and fabricated into tools and cannon. Carding, spinning, and weaving developed. Shipbuilding made possible a direct communication with foreign markets, and lumber, wool, furs, skins, and cotton were exchanged for manufactured goods. New people came to the country; towns increased in size; the movement westward grew in volume. There was an ever-increasing demand for those manufactured goods with which men might meet the difficulties of a frontier life, and might reduce a wilderness to a productive area.

There is no doubt that the rise of the big factory in America was artificially retarded by restrictive laws. The United States was fully half a century behind Great Britain in its industrial development. The Census of 1900, in describing the state of industry at the middle of the Nineteenth Century, says: "It seems probable that until about the year 1850 the bulk of general manufacturing done in the United States was carried on in the shop and the household, by the labor of the family or individual proprietors, with apprentice assistants, as contrasted with the present system of factory labor, compensated by wages, and assisted by power."[2] It is true, however, that there had already been established in Lowell and Lawrence, Massachusetts, certain cotton mills that had reached substantial proportions. Some of these mills were built as early as 1830.

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[2] U. S. Census, 1900, vol. vii, p. 53.

The character of industry has great significance for the distributive organization. In general, the machinery for distributing goods will be modified by the character of the commodity, the character of the manufacturing process, and by the character of the market. It is important, therefore, for an understanding of the distributive system, that one should have some knowledge of the development of industry. On the whole, American industry has borrowed much from British industry. As a matter of fact, American industry is British industry transplanted to a new country and developed and modified by the ingenuity and the independent thinking of the American business man. No sooner had the Declaration of Independence been issued than there began to grow up a system of industry and of distribution of distinctly national character. Simple in its early forms, it became increasingly complex, being compelled to adjust itself to a frontier line that moved ever westward, and to a market ever increasing in size and in purchasing power.

From these simple beginnings, the organization now in existence has risen as the result of evolution. The manufacturing industry outgrew the household, and the small factory developed into the great plant. The distributive system, likewise, grew from its simple, primitive form to the great, complex, nation-wide or world-wide system of to-day. The development of industry and commerce can be sufficiently understood for the purposes of this discussion by calling attention to certain more or less definite stages.

1. The early, simple form of industry and commerce is illustrated by such familiar types as the tin-peddler, the itinerant shoemaker, the meat-peddler, and even by those who carry packs of various commodities to-day from

farmstead to farmstead. Most frequently, it was the maker or producer of the goods that carried them to the consumer. There cannot be a more simple or more direct method than this, but obviously it is not practicable when conditions have become more complex. This may be called the first stage of development.

2. The second stage in the development of our distributive organization came when the producer of goods built his shop and owned his tools, and his customers came to him. This is generally known as the "bespoke," or custom-order, market. The raw material out of which the products were made usually belonged to the customer who brought it to the maker of goods and asked that it be worked up into such products as the consumer required. This was true in the making of clothing and in the making of boots and shoes. Even to-day, there are people who go to shoemakers and ask that shoes be made according to certain specifications. This is a remnant of an earlier period. When industry was in this stage of development, the maker of the goods was also the merchant of the goods. As a matter of fact, he largely sold his services, his skill, and his knowledge. He had no stock of goods, and he ran no business risk. Customers came to him because of his reputation as a workman, and because of personal relations. The significant thing, however, is that he was fixed in one place, that he was permanently located and the customers came to him. It was out of such conditions that the factory and the store developed, because the shop of the shoemaker or of the clothing maker might become either a factory or a store.

3. The third stage in the development of modern business organization may be called the retail-shop stage. This term means that the maker of goods found a larger market than formerly existed among his friends and neighbors who had brought their raw material to be made up. The

maker of goods at this stage of business development began to anticipate the market, and to manufacture goods before he sold them. Out of this situation there came, very naturally, to be a distinction between the maker function and the merchant function. There are other significant characteristics of this new situation. When a producer makes goods before he has sold them or has received an order for them, there arises the beginning of a stock plan. It is necessary for a manufacturer to determine the style of goods and the size of goods that will probably be demanded. In order that he may develop a stock plan intelligently, he must know beforehand what sizes and what styles will likely be asked for. But probably more significant still is the fact that when he had stock on hand and a customer came into his shop to buy goods, there arose a price bargaining. It is clear, then, that this manufacturer was also a merchant and had become a price bargainer.

4. The next stage in the development of modern business organization may be called the wholesale-order stage. At this point in the development of business, there was a large stock of goods on hand. The manufacturer of these goods had made them in large lots in accordance with orders previously received from a merchant who undertook to sell them. This means that there was an earlier anticipation of the market demand. The goods were turned over in large or wholesale lots to an individual whose sole function was that of a merchant. Since he sold the goods in small lots to the consumer, he was called a retailer. In this stage there were two price bargains; one between the wholesaler and the manufacturer, and the other between this wholesale merchant and the consumer.

In connection with this type of business organization, there arose a distinction between the wholesale merchant and the retail merchant. The functions of wholesaler were to buy from the manufacturer in large lots, running the risk of selling these goods at a profit to another merchant who sold them to the consumer. Another added price bargain began. There was the price paid by the wholesaler to the manufacturer, the price paid by the retailer to the wholesaler, and the price paid by the consumer to the retailer. Obviously, as the process became more complex, it was necessary for the producer to make his goods a longer time before they were sold. There was then a longer and greater risk for all those who handled the goods. If the manufacturer made only upon order from the wholesaler, he was comparatively safe. But he thereby lost connection with the market. If the wholesaler sold only to the retailer, he likewise lost connection with the consumer. It is clear that in this situation, the retailer stands squarely between the wholesaler and the consumer, and the wholesaler and retailer divide the manufacturer from the consumer. Thus, the retailer became of greater and greater importance. He alone knew at first hand the consumer market. He alone was in the position to know definitely the changes in wants among consumers. It was he who was in a position to forecast most definitely what the market would need. It was through him that the orders came to the wholesaler.

5. The fifth stage in the development of modern business organization may be called the wholesale-retail-speculative stage. The wholesaler now buys goods in anticipation of the market demand. He speculates. So does the retailer. Here, there are other price bargains. As before, the first price bargain is between the manufacturer and the wholesaler; the second is between the wholesaler and the retailer; the third is between the retailer and the consumer. In this stage, the risks of business squarely rest upon the wholesalers and retailers, and the manufacturers are free from risk only in case they wait for orders to come to them.

This condition has been greatly modified in late years because the manufacturer also has speculated as to what the market will demand. To-day, the up-to-date manufacturer pre-plans his work. He sets his task for six to twelve months ahead and makes goods which he anticipates the market will demand. One manufacturer set his tasks for five years ahead, and he has worked according to the details of that plan ever since.

But upon what basis can the manufacturer pre-plan his work? It is only upon his knowledge of the market. This knowledge of the market he can receive only through his sales organization or the middlemen who deal with him. As long as the wholesaler and retailer stand between him and the consumer market, he must rely upon their judgment. Not satisfied with such a situation, the manufacturer may endeavor by every means at his disposal to secure independently information as to the trend of market demand. The important consideration, however, is that when the producer makes goods and the middleman buys goods, before they have been ordered, they must all share the speculative risks of business. As the condition now stands, therefore, the risk in modern business is shared by retailers, wholesalers, and manufacturers, all of whom are attempting to guess what the consumers will ask for. Risk of this sort always leads to an attempt to control the demand, and out of this condition has come the effort by the manufacturer, by the wholesaler and jobber, and by the retailer, to control the consumer market.

These, in general, are the stages in the development of industry and trade in the United States. There are some specific points to be noted in regard to the rise of the middleman in the organization to handle manufactured goods. In the first place, the importer was usually the wholesaler until after the War of 1812. Even up to the period of the Civil War, most wholesalers did an importing business.

"The organized system of distribution as it existed up to 1860 included importers, who supplied various foreign-made goods; brokers, who marketed the products of the New England textile mills; wholesalers, who were sometimes importers, as we have seen, and who otherwise purchased from importers, brokers, commission men, and from producers direct; and retailers."[3] Until after the Civil War, it was the business custom also for retailers to go to the wholesale centers once or twice each year to purchase their goods. Commercial travelers have developed since the middle of the Nineteenth Century.

It is clear that the development of the distributive system was first toward complexity. The variety of goods was greatly increased and, as the markets grew in size and importance, men confined themselves more and more narrowly to a specialized function. There came to be, therefore, fairly distinct types, such as wholesalers, brokers, jobbers, commission men, factory agents, and retailers. Varieties of goods greatly increased in number. It is a significant fact that in the average grocery store of to-day there will be found from 750 to 1,000 different brands of goods. Large grocery stores often carry as many as 5,000 different brands.

Another characteristic of the earlier period in the development of the distributive organization is the fact that the merchant was generally a passive agent. The customers came to him to purchase their goods. This was in the days before the advent of traveling salesmen and drummers and advertising. In the later stage of development, however, there has been a tendency toward simplicity. In general, the distributive organization to-day for handling manufactured goods is simpler than the organization for handling raw materials and farm products. It is important to inquire the cause of this tendency toward simplicity.

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[3] Nystrom, *Economics of Retailing*, p. 30.

The chief factors making for a simplification of the distributive organization are: (1) the development of large-scale production; (2) the standardization of goods; (3) the assumption of different functions by dealers and manufacturers.

With the tremendous increase in market demand, due to an increase in population and in purchasing power, and with the standardization of machine processes in production, there developed what may be called large-scale distribution. There are jobbers to-day who have as many as 300,000 accounts upon their books. There are many distributive organizations that cover the entire country. Retailers in large trade centers do many millions of dollars' worth of business every year. As the volume of goods which they handled increased, as these goods became standardized by trade mark and trade name so that they could be sold by sample or by description, their distribution became a simpler problem. With this increase in the volume of business came an increase in the number of manufacturers and dealers.

**201. Channels of Distribution.**—There are several channels open to the manufacturer for securing distribution of his goods. The one which he may select will be determined largely by the character of the commodity which he makes and by the market which he supplies. Even here, however, business custom will be a considerable factor.

The simplest form of distribution is from producer direct to consumer. In this case, the sales may be made by mail. A manufacturer of stoves, for example, sells his goods direct to consumers by means of a catalogue. But the producer may distribute his goods through salesmen and canvassers. Manufacturers have found that college students may prove themselves to be efficient salesmen during their summer vacation. Aluminum kitchen utensils have found a nation-wide sale through this medium. Whether this method will be selected or not depends upon the effectiveness to which it can attain. In certain cases, however, it becomes necessary for the manufacturer to maintain control over his commodity until it reaches the hands of the consumer. In this case, he will seek this simple form of organization. Experience, however, has not demonstrated that costs of distribution have been greatly reduced by this means.

Another type of distributive organization is that in which the producer sells direct to the retailer. This type of organization has a variety of forms. The manufacturer may sell without restriction to all retailers who care to handle his commodities, or the manufacturer may restrict his sales to exclusive retail stores. The manufacturer may establish his own retail stores and reach the consumer through them. Some manufacturers sell to mail-order houses or other consignment agencies.

Whether or not the manufacturer will employ this type of distributive organization, and what variety he will employ, will depend upon the character of the commodity and the character of the market. The large bakers in the cities sell their bread direct to retailers. It is claimed that with such a product and such a market, it is necessary for the manufacturer to maintain direct connection with the retail trade. The baker is always in a relatively close proximity to his market. Bread is a perishable commodity and is presumably to be eaten fresh and, therefore, must be distributed daily. The producer must be in a position to supply bread on short notice. Variations in demand are strong and of substantial proportions. The capacity of market demand must be gauged instantly. The baker, therefore, can operate successfully only through close connection with the trade. The wholesaler and the jobber are thus automatically eliminated.

Another type of distributive organization is the one where the producer sells to the wholesaler, the wholesaler to the retailer, and the retailer to the consumer. In this type, too, there are several varieties. The manufacturer may sell through any wholesaler who in turn is left free to sell through any retailer. Or, the producer may reach out to absorb the wholesale function, thus creating his own territorial agents, who are free to sell to any retailer. Again, these territorial agents may sell to exclusive agents.

In practice, it is largely a matter of individual policy, or even of temperament, on the part of the manufacturer, as to whether or not he will use this type in any of its varieties. It is most complex in character and ought to persist only because it is economically effective. The estimate has been made that 90 per cent of groceries pass through the hands of jobbers. In the marketing of textile goods the jobber is a very important factor. "A study of retail conditions in the dry goods field shows at least one thing with perfect clearness. The jobber performs an essentially economic function. We hear much talk of the elimination of the jobber; but there is no other expedient method for the distribution of a very large part of the dry goods merchandise."[4] It has been stated, on the other hand, that the jobber will have to go; that there is no place for the big jobbing concern.

A large manufacturer of paint, with a national or even an international market, sells his products to exclusive retailers through his own territorial agents. In this case, it works successfully. The manufacturer of a breakfast cereal deals through jobbers who handle for him hundreds of thousands of small retail accounts. He is able to compete successfully with mail-order houses and other distributive types, even including a nation-wide chain-store system that makes its own breakfast food.

Farm implements are marketed through three main channels. Some manufacturers sell through branch houses to farmer agents, to specialty dealers, to automobile dealers or garage men, or by blockmen and canvassers in coöperation with implement dealers, to the farmers. Other manufacturers sell through distributors to implement dealers, farm agents, specialty dealers, or automobile dealers and garage men to the consumers. In competition with these methods of selling, there are manufacturers that sell by mail direct to consumers. Direct selling, it is claimed, is likely to prove too expensive for success. Mail-order business, therefore, will probably not be an important factor. Farmer agents are, as a rule, not effective sales agents, and often ruin a manufacturer's market through price cutting. The only apparent ultimate solution is to be found in building up an independent retail organization through specialty dealers.

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[4] *The Merchandising of Textiles,* p. 28.

An added link may be placed in the distributive chain of this last type. A selling agent, an importer, a broker, or a commissioned agent may be interposed between the manufacturer and the wholesaler. In the marketing of cotton and woolen goods there are commission houses which help to finance the mills and sell their products. A commission house may represent from five to fifteen mills. This middleman institution is found in all kinds of textile trades and also handles other articles that are sold through dry-goods stores.

In the shelf-hardware trade, the manufacturer's agent is a prominent factor. The reason for the existence of intermediaries between hardware manufacturers and jobbers is found in the fact that many hardware manufacturers confine their attention to single articles, or single lines of articles. For example, one manufactures nothing but scissors, another saws, another wrenches, and so on. Furthermore, many such manufacturers have relatively small outputs, and a good many of them are located at a distance from market centers, so that they find it difficult to keep in touch with trade conditions.[5] This agent will handle the business for several different manufacturers, never as a rule acting as an agent for manufacturers in directly competing lines. Usually the agent charges a commission on his sales to repay him for his services.

Brokers may be found in many lines of goods. They are of substantial importance in the canned and preserved-food trade. There are three parts to the distributive system for food: the first may be called the distributive machinery for the primary markets, which carries the goods from manufacturer or producer into the large trade centers; the secondary market is the wholesale system; the tertiary market consists of retailers. It is in the secondary, or wholesale, market that the broker operates. The unbranded staples have most need for a broker. Usually a general broker handles such goods. Specialty brokers handle branded goods. In general, the broker's functions are to serve as adviser and arbitrator, as assembler, and as financial agent. He has a dual responsibility: (*a*) to the manufacturer, to sell at an advantageous price, and (*b*) to the jobber, to afford him an opportunity to buy at a convenient time and place. He will need to struggle to keep his place.

Even in such a relatively simple organization as that which exists for the distribution of wrapping paper, a few brokers may be found. The broker is, however, for the most part a *persona non grata* to manufacturers and jobbers; they both consider him an excrescence, and probably with the development of trade associations and the "get-together" meetings between manufacturers and jobbers, he will be eliminated. The influence and the volume of business done by the broker are decreasing in the distributive organization for handling of finished products, because it is becoming more and more effectively organized. The broker becomes a useless appendage when the jobber or the retailer can meet the producer.

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[5] Weld, *Quarterly Journal of Economics,* August, 1917, p. 579.

**202. Choosing Proper Agencies.**—The problem of selecting the most effective distributive medium involves a study of the commodity and its market, actual and potential. There is also the consideration of the volume of business that is done or sought. The fundamental question to answer in regard to the service of all middlemen is whether or not the amount of business done will justify the assumption of middlemen's functions. In so far as they have knowledge, men do what pays them best. Many manufacturers lacking imagination and perspective drift along old-established channels. Others beat out for themselves new paths to market. A manufacturer of typewriters had the courage recently to break away from precedent in the channel of distribution for his products. He dismissed 15,000 salesmen and agents and abandoned branch offices in 50 cities, and has undertaken to sell typewriters by mail direct to consumers. When a manufacturer of wagons dismissed his agents in the small towns throughout the region where his product was sold, and tried the direct-by-mail sales method, he met with disappointment.

If the goods to be marketed are shopping lines, they must be on hand in shopping centers. If they are convenience or emergency goods, they must be placed in convenient places or where they can be had in an emergency. Certain products require specialists as salesmen, such, for example, as cash registers, comptometers, automobiles, and so on. The distributive organization must provide them. The character of the commodity must always be an important consideration, and yet the same commodity can be marketed under competition with apparently equal success by different methods. Flour, for instance, is sold direct to retailers through branch offices; it is also sold to jobbers; it is sold to brokers who sell to jobbers, who in turn sell to retailers or to brokers; it is sold direct to bakers by flour millers. The same manufacturer may use more than one method at once. He may sell special grades to bakers, branded varieties to large retailers, and different kinds to jobbers and brokers.

As the manufacturers assume the functions of middlemen, they must necessarily develop a sales organization. This means that the market must be reached by salesmen carrying a single line of goods. A jobber, for instance, can carry many lines, as in the hardware trade, and reduce the sales expense. The manufacturer, therefore, must ask himself the question as to whether or not he can afford the expense of duplicating an organization already in existence, established by wholesalers or jobbers. He must also consider the fact that the wholesaler or jobber carries many lines besides his own, while the organization established by himself would concentrate on what he has to sell.

The whole problem of selecting the most effective channel of distribution resolves itself into the following considerations:

1. The character of the product.
2. The volume of business.
3. The size and character of the market.
4. Financial considerations.
5. The problem of service to consumers.
6. The problem of credits.

Through all of these problems there runs the pervading influence of consumer demand. One manufacturer may be willing to take orders from a wholesaler or a retailer, leaving a full knowledge and control of the market demand to him. Another may decide to reach out toward the market himself. The strategic point in marketing finished goods is consumer contact. Consumer demand must be directed toward and tied to the products of a given producer before he can gain the desired control. Hence, the rise of branded goods, trade-marks, trade names, and advertising.

**203. Types of Trade Organization.**—There are various channels of distribution that are employed by the manufacturers of shirts and collars. For high-grade shirts and for practically all collars the line of distribution runs from manufacturer to retailer. Jobbers were formerly a more important factor here than at present; the manufacturers have reached past them to the retailer. In work shirts and in low-priced lines the jobbers have more nearly held their own. Some manufacturers sell direct to mail-order houses, and a few sell direct to the consumer.[6]

In the hosiery industry, the manufacturers sold only to jobbing houses, who in turn sold to the retailers. The major part of this line of goods is still handled by jobbers, but there is an increasing volume of business done by manufacturers directly with the retail trade. In the East and South, manufacturers are still using jobbers and commission houses. This change in selling method has developed along with the development of brands for hosiery.[7]

In the women's muslin underwear trade, there is likewise a tendency to eliminate the jobber. Manufacturers are rapidly turning directly to the retailer. Business with mail-order houses is also rapidly increasing in volume. "Several causes have been instrumental in determining this condition, probably the principal one being the rapid change in styles during the last few years. This has had a tendency to cause smaller and more frequent orders, and the consequent effort of the manufacturer is to get as close to the consumer as possible. It was stated that some establishments have solicitors who go even to the residences of individual consumers.''[8]

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[6] Bureau of Foreign and Domestic Commerce, Miscellaneous Series, No. 36, p. 100.

[7] Bureau of Foreign and Domestic Commerce, Miscellaneous Series, No. 31, p. 158.

Wrapping paper finds its great market among retailers, such as department stores, mail-order houses, and other big users of paper. In most cases it goes through only one middleman, the jobber. There are instances, however, where it passes through the hands of a broker, a jobber, and a peddler before it reaches the consumer. Usually the manufacturer sends his representatives to the jobber, and sometimes to the large consumers. Such agents solicit orders for future delivery from the prospective clients. The manufacturer reaches the broker and resident mill agent through correspondence. The broker differs from the mill agent in that he represents several manufacturers, while the mill agent represents but one. The large jobber has a sales force that calls on the trade daily; the small jobber is usually a peddler himself. This latter dealer calls at the jobber's warehouse and gets his load of paper, daily, and carries his goods from place to place, selling for cash. He is an itinerant dealer, calling on those small consumers whose trade the large jobber does not desire. When the distributive system becomes better organized, this peddler will give way to the more economical jobber. A little paper is sold directly to the largest consumers.[9]

A generalized method of marketing shelf-hardware is shown by the accompanying organization chart. In outlines it is simple, but it shows that manufacturers have in this case also found a way past the jobber to the retailer. It is to be noted that the most conspicuous figure in this type of organization is the jobber. The reason for this fact is said to be that such a variety of articles is included in the hardware line that no single manufacturer can produce them all. Many different factories are required. Automobile tires, tinplate, and paints, not to mention the different kinds of cutlery, can be made more efficiently by several plants. Hence, there must be some agency for concentrating them. This function is performed by the jobber.

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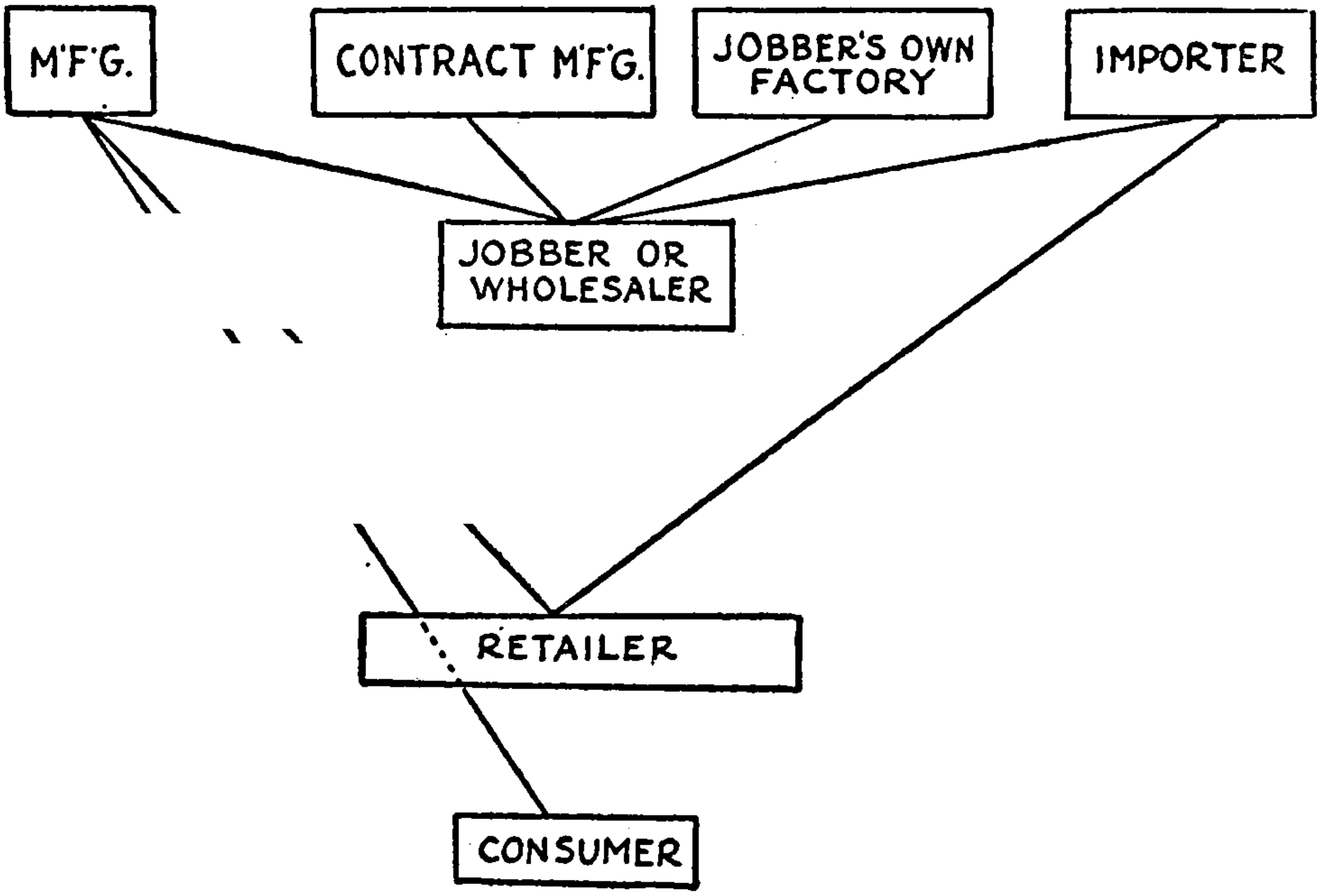
[8] Bureau of Foreign and Domestic Commerce, Miscellaneous Series, No. 29, p. 124.

[9] Cf. Levine, *Marketing Wrapping Paper.*



MARKET ORGANIZATION CHART FOR SHELF HARDWARE

Furniture reaches the market by several different routes. The most important, from the standpoint of the volume of business, is the method of marketing the goods directly from the manufacturer to the retail dealer. It has been estimated that approximately 75 per cent of all the furniture output is sold directly through the factory's own sales force. Furniture is also sold through mail-order houses, through chain stores, and even through "from-factory-to-family" methods. Sometimes factory representatives or selling agents exhibit samples in showrooms where dealers come to buy. There is also a peculiar type of distribution that may be called jobbing. A company may rent furniture-exhibition rooms, may buy outright from manufacturers and sell outright to dealers. It thus performs the functions of assembling, sorting, and distributing in small lots. The same arguments apply to the jobbing function here as in shelf hardware.

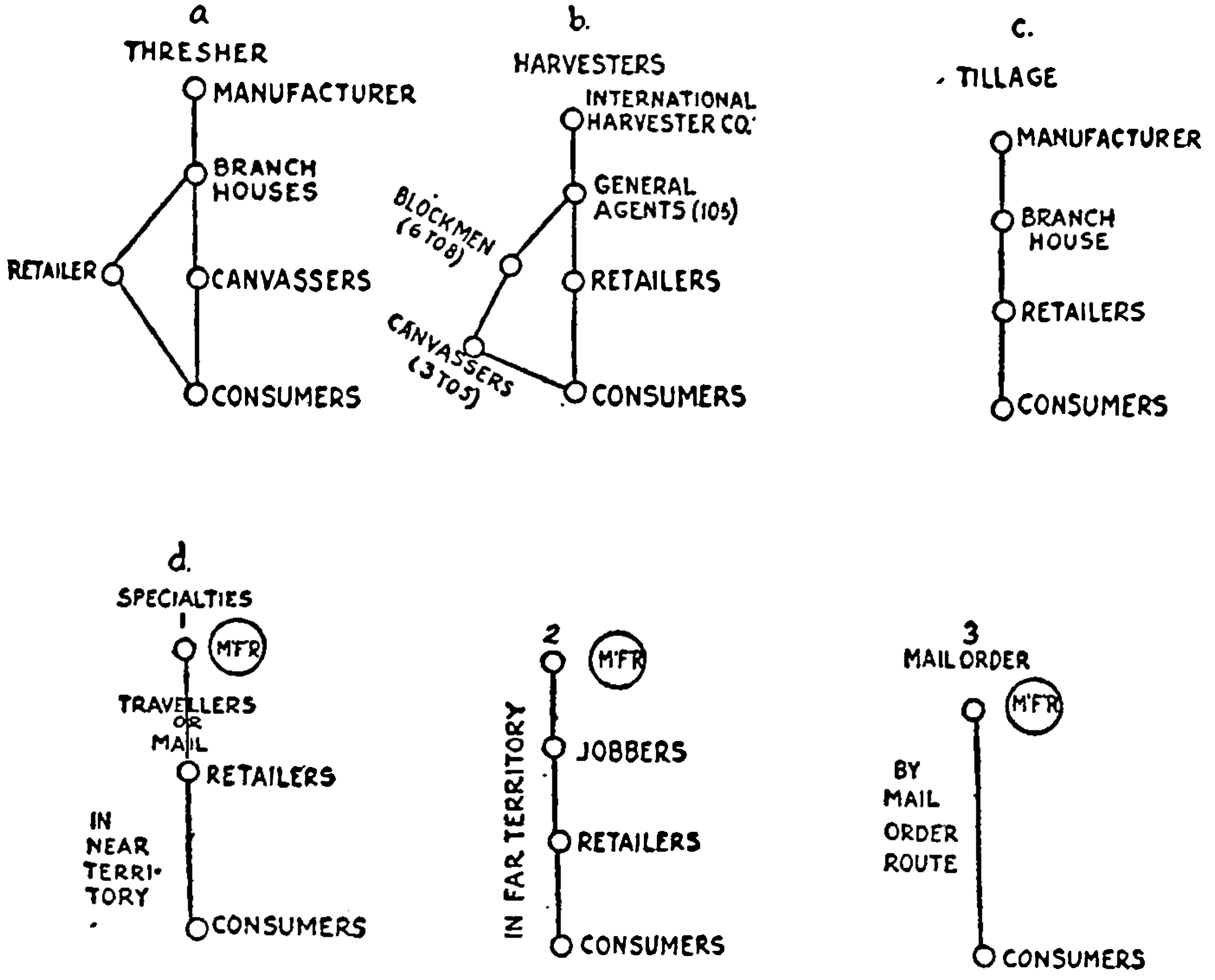
The fact that different commodities, even in the same line of goods, may find different channels to market, may be illustrated in many ways. A certain wood varnish was at first sold through paint dealers, where it seems logically to belong. It was later tried through drug stores, but now meets its greatest sale through grocery stores. A manufacturer of furniture also makes humidors. He has found his best medium of distribution, not through furniture dealers, but through cigar stores.

The case of agricultural implements is one in point. In each instance shown in the accompanying chart the character of the commodity in its relation to the market, together with business tradition, has determined the type in use.

The typical trade organization for handling typewriters is to sell through manufacturers' agents located in all the large trade centers. In foreign business there are also many branch offices. Recently, however, as already noted, a new kind of distributive organization has appeared in the market. In the case cited there has been a distinct attempt to eliminate all salesmen, and all agents and agencies. The offices in 50 cities have been disbanded; 15,000 salesmen and agents have been dismissed. The underlying idea in this new type of trade organization is to escape the evident evils in the typewriter sales organization, the most important of which have been a subsidizing of business colleges and the acceptance of old machines in part payment for new ones. The new method is to sell direct to the consumer by mail, on the ground that this machine is sufficiently standardized, sufficiently reliable, and sufficiently well-known to be sold by description rather than by inspection.

The appeal in this new method is distinctly on the basis of price.

In the marketing of certain household electrical appliances there are four different channels of distribution in use. These articles are sold (1) direct to a jobber, through a "central station" or through a dealer to the consumer; (2) to the "central station" through a dealer to the consumer; (3) to the dealer outright; and (4) direct to the consumer. By "central station" is meant a power plant for generating electric current. Generally the goods are not sold direct to the consumer unless the money accompanies the order; otherwise the order is turned over to a dealer. In this type of organization the jobber is holding his own, the manufacturers leaving to him a study of the market, credit risks, and sales management.


a
THRESHER
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RETAILER
CANVASSERS
CONSUMERS
b.
HARVESTERS
INTERNATIONAL HARVESTER CO.
GENERAL AGENTS (105)
BLOCKMEN (6 TO 8)
RETAILERS
CANVASSERS (3 TO 5)
CONSUMERS
c.
TILLAGE
MANUFACTURER
BRANCH HOUSE
RETAILERS
CONSUMERS
d.
SPECIALTIES
1
M'F'R
TRAVELLERS OR MAIL
RETAILERS
IN NEAR TERRI-TORY
CONSUMERS
2
M'F'R
JOBBERS
RETAILERS
IN FAR TERRITORY
CONSUMERS
3
MAIL ORDER
M'F'R
BY MAIL ORDER ROUTE
CONSUMERS

MARKET ORGANIZATION CHART FOR FARM IMPLEMENTS

These examples of trade organization will illustrate various phases of the distributive problem. It will be seen that in most instances there is a trend toward further simplification; the aim is to have goods move as directly as possible to the consumer. In marketing manufactured products costs are constantly running against them until they reach the consumer. Every middleman has his costs of operation and his profits to cover. The longer the time that the goods are on the way, the higher the interest charge for financing them. With improved facilities for communication and for transportation, the retailer may buy more nearly direct from the factory and more frequently, and the manufacturer may be in a better position to reach the consumer market. But the most important influence for change is to be found in the struggle between the large manufacturer, the large jobber, and the large retailer, for a control over consumer demand.

**204. Chaos in Trade Organization.**—There are strong influences making for radical changes in methods of selling finished goods to-day. These are primarily due to the new status of certain manufacturers, jobbers, and retailers, which has the following causes. The great increase in the market, with a rapidly developing country and a population increasing fast both in numbers and purchasing power, made for a much larger volume of business. Certain manufacturers found themselves in advantageous positions in this expanding market and became "big" manufacturers; certain jobbers multiplied their volume of business many times over; certain retailers likewise grew in financial power and in volume of trade.

Under these changing conditions the manufacturers, with their standardized processes and vast output of goods, began to realize that they did not control either the raw materials or the market for their goods. They began then to reach back toward the source of materials and, looking forward toward the market, began to identify their goods by trade marks and trade names. They began to advertise their goods to the consumer in national campaigns.

The jobber, when he realized that the manufacturer was reaching past him, began also to identify the goods which he handled. Some of the well-known brands to-day, in hardware, for instance, and hosiery, are jobbers' names. This middleman found it difficult, however, to sell standardized goods bought from different manufacturers. In some cases, therefore, he reached out to control manufacturing. Just as the manufacturer assumed his function, he in turn began to manufacture. Both manufacturer and jobber appealed to retailer and consumer.

Certain retailers, in their turn, became unwilling to remain passive. In finances they were independent of the jobber; their business justified their buying in wholesale lots. But, in handling goods identified with trade marks and trade names of manufacturers and jobbers, the retailers became more and more mere order takers. Thus, they too put brands on goods and advertised. Their strategic position arose from the fact that they met the consumer face to face.

During recent years these three, the big manufacturer, the big jobber and the big retailer, have been struggling for the control of consumer demand. Their efforts have tended to disrupt existing trade organizations and have on the whole tended toward simplification. Out of this struggle have risen the problems of advertising, of trade-marks, trade names, dealer helps, of defense and offense, that characterize business to-day.

## SUGGESTIONS FOR STUDY

The student should study the trade organization connected with his special commodity. An organization chart will prove helpful in understanding relationships. The following topics will serve for classroom study:

1. Source of confusion in the distributive organization.
2. The problem of exclusive agencies.
3. The character of the commodity in relation to the distributive organization.
4. The relative importance of wholesaler and retailer in controlling consumer demand.
5. The position of the general store.
6. The assumption by the manufacturer of distributive functions.
7. Distributive organization and the market.
8. The future of the jobber.

READINGS:

Nystrom, *Economics of Retailing,* Chap. II.

Cherington, *Advertising as a Business Force,* Chap. II.

Mahin, *Advertising,* Chap. X.

Calkins and Holden, *Advertising,* Chap. III.

MacMartin, "Planning an Advertising Campaign for a Manufacturer," Part III.

*Modern Business,* volume ix, pp. 275-317; 341-350.

Shaw, *Approach to Business Problems,* Chapter II, pp. 9-12, 16.

*Advertising and Selling,* June, 1910, p. 59. "How would you like to be the Groceryman?"

*Printer's Ink,* March 12, 1914, p. 92, "What Agencies are Worth"; April 30, 1914, p. 37, "Exclusive Agencies"; December 18, 1913. p. 34, "Points to Consider in Choosing an Agency."

# CHAPTER XVI

## "NEW TYPE" RETAILERS

In the struggle for control of consumer demand all contestants have advocates. Some say that the manufacturer is in the advantageous position, if he makes his goods known and stimulates inquiry by the consumer for them through advertising. Others say that the jobber can block the manufacturer's way to market and tie the retailer to himself by financial obligations. Still others claim that the strategic moment is the moment of sale, that the retailer alone is in "at the killing," that he meets the consumer face to face and can suggest, advise, and substitute.

It seems clear that, whether or not the retailer has taken full advantage of his position, he has the opportunity to direct demand to a very substantial extent. Especially is this true in the suburban and country markets. The retailer can become a potent social factor in the community, according as he realizes the possible service that he can perform. On the basis of his methods, the retailer will fall into one or the other of two classes: the one is called the regular or old-line retailer; the other is called the "new type" retailer.

**205. Regular vs. New Type Retailer.**—The regular retailer is the one who keeps his place, *i.e.*, from the point of view of the jobber and manufacturer. He is more or less passive, doing on occasion desultory local advertising, but attending strictly to a retail business. Goods come to him through the regular channels of trade. He makes his annual or semi-annual trip to the wholesale center for the purchase of his season's supply of goods; or he buys from the drummers, or traveling salesmen, who visit him. In a word, he remains true to the type that developed with the older system of distribution.

The institution through which the regular retailer has functioned most typically is the "general store." This was the frontier retail institution, with a prototype in army trading and "company" posts of pioneer days. The general storekeeper was the merchant of the early community. He kept, in so far as he could, what the community needed, and made out of his store a veritable Pandora's box. As the frontier line moved on, the general merchant remained. His tribe multiplied as the posts grew into towns. From the primitive carry-all store, which was likewise a social center, there developed certain specialty stores, such as the drug store, hardware store, dry-goods store, and so on. All of these remained regular so long as they kept within the bounds of retailing.

With the growth of trade centers, however, new functions were assumed by those retailers who possessed ability and saw the advantage of combining other distributive functions with retailing. There arose a group of merchant princes in retailing, whose courage, daring, originality, and shrewd judgment brought changes into the old system. These new business leaders have organized new institutions, and have come to be known as the "new type" of retailers. Their methods can best be understood through a study of the department store, the mail-order house, the chain store, and the manufacturer's branch. Another attempt to combine distributive functions is found in the coöperative store.

**206. The Department Store.**—"Woman is a shopper" says one writer on business, "hence, the department store." By this he meant that the foundation of the retail establishment known generally as the department store is based upon shopping lines of goods. The basic commodity is generally accepted to be textiles. However, whether or not that may be true is uncertain, the records at present are not clear. The name itself is derived from the type of organization. A department store is an aggregation of departments, each one, up to a certain extent, a little store within itself. If the textile group formed the original core of the organization, many others have been added from time to time. The ideal of such a retail store is to carry everything asked for. A prospective customer, it is claimed, disappointed too often will not return.

Each department within the store has its own individual organization. One man, who is generally called the department head, is responsible for the activities of the given department. The general principle in the direction of department stores is to demand that each department must pay for itself, that each department must obey the rules of the house or business policies, that each one shall be under a central authority, and that each shall work in harmony for the common good. The number of departments varies greatly in different stores. In general, they run from 20 to 250 departments.

The organization within each department is, or should be, clearly defined. Each one has its individual problem of purchasing and of selling. For each, there is a stock plan under the direction of a managing head. It is the general custom for each department head to be entrusted with a given amount of capital to spend. He is allowed to buy and sell with as large a degree of independence as is practicable. To the extent of this independent activity, the department head retains the functions of an independent merchant. His judgment, however, must run along the lines set by the general manager. The terms of sale, the percentage of gross profit, the volume of business, the amount of net profit, are questions for the central management to determine. Orders for goods are usually valid only when signed by a member of the firm or specially designated agent. Individual independence within each department is, therefore, strictly limited by the central management.

With the rapid development of the department store it becomes an important question to ask what goods can be concentrated within it. Is there any economic limit to the extension of department store activities? No definite answer can at this time be given to such a question. The so-called "convenience" lines of goods are the largest in this type of retail store, and it is said that such goods make up half the total business of the rural general store. If the theory of the department store is correct, namely, that it depends primarily upon a shopping line of goods, the conclusion inevitably follows that this principle will determine the extent of concentration of business for department-store retailing.

Many department stores carry groceries. From the point of view of the consumer, this line of goods depends for its economic retailing upon (1) quality of goods, (2) ease of ordering, (3) promptness in delivery. Groceries are obviously "convenience" goods. Hence, on the basis of principle, groceries are extraneous to the evolution of the department store. It is the general opinion of authorities that department stores have not yet made a great success of their grocery departments.

Most large department stores carry furniture. This line of goods is bought as an important item in the family budget. There is usually a family consultation before any extensive purchase is made. The furniture trade is to-day fairly well divided between special furniture stores and department stores. On the theory that women are fond of shopping and men are anti-shoppers, this division would seem to be a natural one. Furthermore, if the department store does in reality depend upon the opportunity for shopping which women demand, furniture can never be controlled wholly by department stores. If, however, articles of furniture come to be regarded from the same point of view as textiles, they may find a natural place in the department store.

There is also a jewelry department in most of the department stores. Usually it is not high-priced jewelry that is to be found in such retail establishments. This is due to the high cost of such goods and to the need of experts in handling them. The specialty store for jewelry has a distinct advantage here. Low-priced jewelry seems to be firmly fixed in the department store and small jewelry stores are becoming repair shops. It is predicted that department stores will never be able to secure the trade of the high-grade jewelry stores.

Several lines of hardware are also to be found in department stores. It may be said that in general hardware is the kind of goods which men purchase. It is to be observed, also, that shelf hardware has tended to remain in specialty stores. Tinware and kitchen utensils, however, are to be found in the basements of most department stores. The same principles apply here as have been indicated before. If there is a change in method of purchase, the department store may incorporate more and more hardware lines.

Among textile goods, there is a line which may be called "men's wear." These articles will prove to be a real test of the principles that have been announced as underlying the development of department stores. If it is true that men dislike big stores with their crowds, if it is true that men incline to buy more or less spontaneously from window displays, it will obviously be a difficult matter to concentrate the goods which they purchase in a department store. Attention has been called to the fact that business men who commute back and forth into New York City buy their clothing in their home towns more frequently than the women in their families.

Business habits are not clearly defined and are never fixed for a long period of time. Every generalization, therefore, must be qualified for the sake of accuracy. According to the principles announced above, however, the department store can concentrate a large share of the shopping lines of goods. It has been able to hold its own in practically all lines against specialty stores. As goods pass from the convenience or emergency group into the shopping line, they will be more fully suited for department store retailing. It is also obvious that many goods will be carried for the convenience of those who come to shop. Men and women will find it convenient to make purchases of other things besides shopping lines, although they may not visit the department store for that particular purpose.

The advantages which the department store claims over the regular retailing establishment are as follows: the department store has a great advantage in the stock plan which it can develop—each department is able to work on its specific stock plan; the department store also has buying advantages; it has advantages in operation which go with large-scale production; it has banking advantages—a large merchant is frequently a better risk than a small merchant, as he usually has sufficient capital to take advantage of all the discounts. As the department store increases in size, it may assume the wholesale function and buy direct from manufacturers. This gives the department store an advantage in speed of turnover of its goods. The range in speed of turnover in cities of first rank throughout the United States is from four to eight times per year. The department store claims also to have advertising advantages. It has been able to secure advantage from bargain prices.

This type of retail store has its weakness as well as its strength. There is no longer the direct, personal contact between management and salesmen. The manager-owner is no longer to be found where the department store has developed. On general principles, a man will not work for others as effectively as for himself. The chief weakness of the department store, however, is in the basis of competition. Investigations appear to show that in general the average cost of doing business in department stores is higher than in small stores. The program has been, in the past, to sell more goods every year, but inevitably the time comes when department-store markets begin to overlap.

When department store competes with department store, it is found that they are practically equal in all points and must compete on the basis of service and good will. To this kind of competition there is no fixed limit. One department store spends five per cent on service alone. The rest rooms, the delivery service, the information office, the parcels check-room, pipe-organ recitals, etc., are evidences of this competition in service. Costs, therefore, increase from year to year. An insidious danger lies here.

The effect of the department store upon methods of retailing has been on the whole good. It has tended to simplify the distributive organization for handling manufactured goods. It has weakened the position and has taken over the services of the wholesale buyer. It has practically revolutionized the retailing business through the introduction of competition in service. It has, to a considerable extent, eliminated the element of personality in retail selling. It has been able to study more fully and more carefully the problem of retailing and has introduced many methods of saving. In order to keep going in business, the regular retailer has been compelled to modify his old-fashioned and wasteful methods.

The future of the department store is, of course, an unsolved riddle. There is no apparent reason why it should not continue to prosper. More and more departments are being added to the large department stores, and more and more goods are passing into shopping lines. This retail establishment has become a vast emporium for carrying goods of all classes and prices. While it is claimed that no store can appeal successfully to more than two grades of purchasers, it is nevertheless an observable fact that the "shawl" trade and the limousine trade are both served by many department stores. Apparently, department stores have risen to meet an economic need. In general, it seems probable that they will endure, unless they destroy one another by too expensive service.

The department-store type of retail establishment is not confined to the United States. A famous Paris store had developed long before the first department stores appeared in this country. It is claimed also that this type of store has found immediate popularity in China. "The Chinese of to-day are fond of novelties. That is one important reason why the Sincere Company has been so successful in Canton and Shanghai. Even more people go to the department store singly or in groups day after day than go to the amusement houses, making purchases of possibly not needed articles. The poor and rich men and women find it a meeting-place, elbowing and shouldering together. It is a sign of the Chinese becoming more democratic."[1]

**207. The Chain Store.**—The chain store as a retail establishment is closely related to the department store in organization. If the "little store within a store" is taken out and put into another section of the city or another city, there is the beginning of a chain. Essentially the chain store is a department store split up into units. It is to be understood, however, that this applies only to organization. All stores in the chain carry practically the same line of goods.

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[1] *Commerce Reports*, January 11, 1917, p. 888.

Chain stores fall naturally into three groups. There are the manufacturers' chains, which are called manufacturers' branch stores. There are also the jobbers' chains, where the chain store idea has been applied to the jobbing business. There is in the third place the retailers' chain. This is by far the most important and is the one which will be discussed here in detail.

The chain store aims to secure all of the buying advantages of the department store and all of the selling advantages of the small retail store. In contrast with the department store, however, where the basis is a shopping line of goods, the chain store relies upon convenience and emergency goods. As has been said in the analysis of emergency goods, the main purpose in retailing is to have the right thing in the right place and in the right quantity at the right time. What the consumer wants he wants quickly. The success of the retail store, therefore, which depends upon convenience or emergency goods, is largely a problem of location. The chain store claims its greatest success in adjusting itself to the requirements of this problem.

Chain stores carry many different types of goods. There are a number of chains which carry groceries. There are at least four extensive chain systems handling notions and generally known as "five- and ten-cent stores." There are tobacco and cigar store chains. There are chain stores handling shoes, and there has recently been added an extensive system of chain stores in hardware. One analysis of experience with chain-store systems reaches the conclusion that they work best in emergency goods, less well in convenience goods, and with difficulty in shopping lines.

The chain store has dealt successfully with groceries, drugs, and cigars. Here it has eliminated the wholesaler and in many cases has absorbed likewise the functions of producer. An important characteristic of the chain-store system is that an organization can retain direct control of goods from source to consumer. It has been associated in the past with various methods of price cutting and other cut-rate methods. Practices of this kind have aroused manufacturers, jobbers, and the regular retailers. Even the suspicions of the consumer have been raised at times, but the desire for a bargain is in many cases strong enough to overcome this suspicion. In purchasing supplies, the chain stores have come with large orders and a demand for special rates. It is probable that they can match the department stores in their buying advantages and in their selling advantages.

Specifically, the advantages which the chain store claims are (1) large-scale buying, (2) a possibility of combining manufacturing, wholesaling, and retailing, (3) a standardization of equipment and of selling methods, (4) the ability to shift stock from one section of the country to another, in order to adjust it to market demand.

There are several varieties of the chain-store system. These stores which emphasize bargain prices are usually called economy stores. Such retail establishments exist in the grocery trade especially and, to a certain extent, in tea and coffee and low-priced notions, or convenience goods. One line carrying groceries has now practically 3,000 stores located in different parts of the country. There has been during the period of increasing prices a very rapid development of these stores. It may be said in general that those stores handling staple goods where price is the determining factor flourish best in hard times or in periods of increasing prices. The general principle of such chain stores is to reduce operating costs by reducing service to a minimum.

The type of chain store usually known as the five- and ten-cent store has had a most interesting development. One of these chains, which has stores in all parts of the country and is to-day probably the largest, was established in February, 1879. This was the first attempt at the chain-store system. In the early years, these stores were a success, but later met with disaster. After struggling along for five years, the idea began to be accepted and growth from that time on has been rapid. From a single store in 1879, this system has grown to 781 stores in the United States, Canada, and England.

In this type of retail establishment, location is undoubtedly the next important item to that of price. It may be said, in general, that the location of the five- and ten-cent store to-day is determined by the following considerations. The experience with such stores has shown that ninety per cent of their trade has been with women. To-day, therefore, such stores are located on what is known as the shoppers' side of the street. Some others are established where rent is cheaper, regardless of convenience of customers. Other factors to be considered in the location of chain stores are the growth of the city, and the securing of conspicuous corners in the cities already developed. The five- and ten-cent store seeks a location as near as convenient to a department store. In this way, it gets the benefit of advertising which draws the crowds to that place. A theater, a drug store, or other attractive store can serve the same purpose. No location is sought near saloons, banks, or places where men alone congregate. Traffic conditions are also considered in the location of these stores. In cities with large interurban railroad systems, a location is made, if possible, at the connecting point. The experience from these stores has shown that an admirable location may be found on cross streets. In this case, it is advisable to have the store located halfway between two cross streets. The important consideration is always where people who are prospective customers are likely to go.

The stock problem of the five- and ten-cent store is always a difficult one. The study of this problem, however, has demonstrated the following facts: that about 92 per cent of the stock is made up of every-day necessities; that about 4 per cent is made up of luxuries; that candy and jewelry novelties make 2 per cent more; and that fads and souvenirs constitute 2 per cent. Besides these articles which go into the regular stock plan there is always an opportunity left for experimental goods. These stores include as many as forty-eight different lines of goods. The ones that have recently been added are groceries, auto parts, a flower department, a photograph gallery, a soda fountain, and a restaurant. It is claimed that the limit of expansion has apparently been reached, although some chains consider adding a circulating library. Expansion must, therefore, come in higher prices rather than in more lines.

In carrying on this type of chain store with profit, it is claimed that there cannot be less than six turnovers of goods within a year. Successful operation demands also an average gross profit of 40 per cent.

**208. The Mail-Order House.**—The department store illustrates the retailer who seeks advantage of large-scale buying and large-scale selling, especially in shopping lines. The chain store illustrates the retailer aiming at large-scale buying and small-scale selling, especially in emergency and convenience goods. The mail-order house or the catalogue house illustrates another attempt to divert from their regular channels goods that are on their way to the consumer. It is to be remembered in this connection that no matter what the type of retail establishment, the same functions are to be performed. The department store then, beginning as the retailer, has reached out to incorporate the wholesaler's functions and is to-day extending even to the factory to control or own it. In the same way, the chain store has often found it necessary to do manufacturing and wholesaling as well as retailing. The experience of the mail-order house is the same. It started out to be a retailer only, but now the largest mail-order houses do wholesaling and manufacturing as well.

The principle upon which the mail-order house has developed has been to buy direct wherever possible and to sell direct to the consumer always. Experience has shown that the mail-order house is compelled to re-distribute profits rather than to reduce substantially the cost of distribution. Operating expenses, however, for retailing in this kind of establishment fall below those of the department store and the chain store.

The mail-order house eliminates the sales force. It substitutes for salesmen a catalogue which may be either general or special in type. This catalogue is the only appeal which the mail-order house makes. This appeal is on the basis of prices. The principal argument by the mail-order house is a price lower than that asked in regular retail stores. Until recently, the mail-order house catalogue carried price comparisons showing that the price of their goods was lower than that of the regular retailers.

Usually the terms offered by the mail-order house are a cash payment with the order. Some such retail establishments, however, have always extended credit. The most distinctive feature is the guarantee which all the large mail-order houses now make to the consumer. One concern offers in large type on the outside of its catalogue: "We guarantee absolute satisfaction. Promptly return to us at our expense any unsatisfactory purchase. We will then either exchange it for what you want, or return the full amount you have paid together with transportation charges." It is said that a guarantee of this kind issued by a large house has a peculiar psychological effect. It not only promotes confidence in the statements made in the catalogue, but it also promotes confidence in the goods themselves, even after they have come to the customer. The guarantee therefore tends to prevent returns and exchanges rather than to increase them.

Mail-order houses have always been notoriously close buyers. Their purchases have been made in large quantities, and usually have increased from year to year. With each increase in purchases better terms were asked by the mail-order houses. When they have become the dominant purchaser of any manufacturer, they can then largely determine his success. In this way they have been able to secure on advantageous terms manufacturing businesses that are already established. There seems to be no essential reason, however, why mail-order houses should have any buying advantages superior to the department store and the chain store. Their peculiar problem in buying is that their catalogues must be made up at least six months ahead of time and goods must be on hand to meet instantly any inquiry that comes in response. In a period of fluctuating prices, the buying problem is peculiarly complicated.

Mail-order houses carry many different kinds of goods. The principle among the largest has been to charge against each department a sum proportionate to the space occupied by its commodities in the catalogue. When an article does not pay its way, it is eliminated. The variety of goods in mail-order houses in the face of this principle has been constantly increasing. Articles that a few years ago would have seemed impossible to sell on description at long range appear to be fixed permanently in these catalogues. These include wagons, buggies, gas engines, cream separators, phonographs, and dwelling-houses. Apparently shopping lines of goods would not be suitable for mail-order houses to handle. Nevertheless, they have not proved to be an insuperable barrier. The essential limitations as to the variety of goods which mail-order houses can handle are to be found in the possibility of describing accurately and of standardizing the commodities. A satisfactory idea of the character and quality of each article must be conveyed to the prospective customer. It is also necessary to establish a standard for commodities, in order that a guarantee may be made. Within these broad limits, there is not to-day any end to the kind of goods which can be sold through catalogues.

Mail-order houses as retail establishments have certain inevitable limitations. It is difficult for commodities to be made attractive in appearance through pictures in the catalogues. There is no chance for the customer to inspect the goods before purchasing. City buyers can get more service from other types of retailers. Also the average customer has difficulty in visualizing an article from a mere description. Furthermore, mail-order houses cannot hope to compete with other types of retailers in offering credit.

The advantages claimed by the mail-order houses over the small local retail stores are as follows: the mail-order method of advertising is far superior and much more effective than that of the average local retailer; the extreme care used in descriptions and in pictures is also to their advantage in this regard; the large mail-order house is enabled to offer through its catalogue a very wide variety of goods. In this respect the small-town merchant cannot compete. Moreover there is the feeling on the part of the average customer in rural districts that goods bought from the large trade centers are of superior quality.

The large mail-order house, furthermore, through its financial power and its ability to market immense quantities of goods, is able to buy much of its merchandise at inside prices which often are so low that the mail-order house may undersell its rural competitors and still make a good profit. Like the department store and the chain store, the mail-order house has been a potent factor in toning up retail business. Its effect has been felt more strongly in the country retail business than in the cities. There is no doubt that the mail-order methods of doing business have done much to tone up the country retail trade. These catalogue houses have also educated the country trade to greater consumption. They have demonstrated the possibility of selling all sorts of goods at long range and by description.

The essential characteristics of mail-order business are a standardization of goods, an iron-clad guarantee of consumer satisfaction, the payment of transportation and delivery charges by the customer, and sales made through the mail. Many large stores of the department-store type and of the specialty-store type do some mail-order business. Their main volume of trade, however, depends upon customers who come to their stores to inspect the goods and to buy across the counters.

The future of the mail-order business appears to be one of prosperous development. A recent writer on this type of retail business has declared: "To me, the value of the mail-order method of distribution seems so great and so easily demonstrable that I refuse to believe that it will not appeal to the great majority of the American people who, whether they live in the city or the country, are daily becoming more intelligent in their study of life's problems."[2]

**209. The Manufacturer's Branch Store.**—The special type of the chain store established by the manufacturer is known as the manufacturer's branch store. The general type of chain store is a retail establishment in origin. This type is an extension of the control of the manufacturer over the distributive process. He is now a manufacturer, a wholesaler, and a retailer. The kinds of goods adapted to this method of retailing are illustrated by sewing machines, cash registers, farm machinery, typewriters, and automobiles. The policy which governs the organization of this store is one to control the commodity from the manufacturing plant to the consumer. It is also clear that connected with the commodities named above, there is need for expert sales agents who can educate the consumer in the character, the methods of setting up, and the operation of machines.

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[2] *The Outlook,* June, 1916.

It is not essential, however, with such a system of retailing, to handle commodities of this character. There are manufacturers' branch stores which carry shoes. Some of the well-known brands of shoes are distributed in this way. Clothing of certain brands, also, is handled by a series of manufacturers' branch stores. The two chief characteristics of these commodities are special service and special risk.

The advantages claimed for the manufacturers' branch stores are: direct control of goods from the plant to the consumer; ability to shift stocks of goods from one section to another; a direct channel for securing knowledge of consumer demand; and a standardization of equipment. The difficulties in the successful operation of such a system of distribution are the same as those connected with chain stores. It is hard to find branch managers who can run the business successfully and whose judgment and activities can be controlled by the central management.

There are no problems to be found in the manufacturers' branch stores which are fundamentally different from those that have already been discussed in the chain-store system. This method of distribution has not developed rapidly and there is no prospect that it will become, in any sense, a dominant factor. Some manufacturers have achieved success with this method, but others have reached equal success by other methods. Apparently it has no permanent superior features.

**210. Cooperative Stores.**—Another method of simplifying the distributive organization is through coöperative effort. The most successful experiment in this method is found in the coöperative buying and selling of citrus fruits. It is interesting to note in this connection that the California Fruit Growers' Association has undertaken to sell its products by the same methods that are used in the selling of manufactured goods. They have standardized their products and they have identified them with trade marks in the same way that manufacturers have done with their goods.

In general, coöperative effort has not been a decided success in the United States. The essential difficulty has always been to secure efficient managerial help for the coöperative stores. In certain localities where there is a clearly defined social group, the coöperative retail store has been a success. For the most part, however, the coöperative organizations have not been able to compete in the open market with other retail establishments.

In a recent report made by the Department of Agriculture on the success of typical coöperative stores in the United States, the following conclusion was reached:

> Owing to the fact that the enactment of coöperative laws in the different States is a comparatively recent movement, a large proportion of the stores examined were originally established under the ordinary corporation laws. Most of them, however, are now organized under coöperative laws. At the time of this survey such laws had been enacted by 30 States, including all of the States covered by this study. Thirty-two out of forty-two of the stores reporting on questions were then organized under special coöperative laws. Those which still retained the corporate form of organization adhered to certain coöperative principles which were made a matter of agreement between the

members through their constitution and by-laws. For example, 40 of the stores had adopted the principle of 1 man, 1 vote; while 5 of them adhered to the plan of voting according to investment. It was noticed, however, that in the older associations established under the corporate law there was a tendency for the stock to pass into a few hands, and in several of these cases the store was coöperative only in name.

Although the figures were not conclusive, nor sufficient for tabular presentation, they seemed to bear out the opinion of many of the managers that a coöperative store is apt to be more successful in a community which is made up of people of one nationality. Similarly, in industrial communities, it was found that stores are more successful where a large percentage of the membership is of the same occupation; and at least one case was observed in which common church affiliation is the basis of successful operation.

The membership ranges from 1,600 to 30, while the average for all the stores surveyed was 228. Although there were some notable exceptions, as a general rule it was found that the success of the stores was almost in direct proportion to the membership. This may be due to the fact that the well-managed store usually has little difficulty in increasing its membership, while the poorly managed store soon loses the support of the members with which it begins operation. . . . The causes of failure, it is evident, are largely the opposite of those conditions which make for success. The converse of the safeguards for success would be (1) lack of leadership; (2) poor management; (3) unfavorable environment; and (4) lack of proper legal precautions. . . . Briefly stated, the conditions of success may be summarized under the headings: (1) leadership; (2) capable management; (3) favorable environment; (4) adequate legal safeguards.[3]

**211. Cooperative Buying.**—An attempt to secure the advantages of coöperative effort is to be found in organizations of retail merchants who have combined for advantages of large-scale buying. In one town in Iowa, for example, there are 500 merchants who compose the Retail Commercial Union and who are backed up with the combined annual buying power of $40,000,000. The plan of this organization is to place large orders at one time with manufacturers. It claims that exceptional price advantages are certain when purchases amount to more than five hundred times that of a single store. No doubt such combined purchasing gives a distinct advantage to the retailer.

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[3] U. S. Department of Agriculture, Bulletin No. 394.

**212. Conclusion.**—These are the types of retail methods that have developed during recent years in the distributive organization. The power of the department store, the mail-order house, and the chain store has become sufficiently great to make them a potent factor in distribution. They are to-day undoubtedly the leaders in business methods in retailing manufactured goods. In many respects they have taken advantage of large-scale organization, of reducing costs, and of controlling the course of commodities.

It is the struggle between these great retailers, the large jobbers, and the large manufacturers that is the determining factor in the shaping of a new type of distribution. They all have ample financial backing, they are all able to appeal through national advertising to the consumer. They have all identified the goods which they handle by trade-marks and trade names. They have likewise endeavored to absorb all the functions of manufacturer and distributor. The character of the future distributive organization will largely be determined by these business men.

### SUGGESTIONS FOR STUDY

The student should, at this point, study the type of retailer who handles the commodity he is investigating. The following topics will serve for classroom discussion:

### *The Department Store*

1. The origin of the department store.
2. The rise of the department store.
3. The organization of the department store.
4. The alleged economic advantages of the department store.
5. The limitations of the department store.
6. The future of the department store.

### *The Chain Store*

1. Growth and development of the chain store.
2. The organization of the chain store.
3. Its economic advantages.
4. Its future.

### *The Mail-Order House*

1. The origin of the mail-order house.
2. Economic reasons for its success.
3. The mailing list.
4. The catalogue.
5. The mail-order house and distribution.
6. The mail-order house and the rural store.
7. The mail-order house and the city trade.
8. Credit problems of the mail-order house.

### *The Coöperative Store*

1. The economic claims for the coöperative store.
2. Coöperation and American business men.
3. Organization of the coöperative movement.
4. The future of coöperation.

Readings:

Nystrom, *Economics of Retailing,* Chaps. XII, XIII, XIV.
Fisk, *Retail Selling,* pp. 24-26.
Cherington, *Advertising as a Business Force,* pp. 158-204.
*Selling Forces,* pp. 103-132.

Wanamaker, *Golden Book of Wanamaker Stores*, pp. 133-181.
*Printer's Ink*, 1913: April 17, p. 12; November 13, p. 41; 1914: June 4, p. 45; June 11, p. 12; June 18, p. 85; July 9, p. 3; August 6, p. 60; September 7, p. 23 and 63; October 8, p. 36; October 29, p. 72; November 5, p. 58.
*Outlook*, January 7, 1916, p. 227.
Mahin, *Advertising*, Chap. XIV.
De Weese, *Practical Publicity*, pp. 118-125.
*Annals of the American Academy of Political and Social Science*, vol. 1, pp. 223-39.
U. S. Department of Agriculture, Bulletins No. 394 and 301.

# CHAPTER XVII

## BUSINESS POLICIES

**213. What the Business Policy Is.**—The skill, intelligence, and individuality of the business man are nowhere shown more clearly than in the rules, regulations, and policies which he formulates for his own business. A "house policy" is, therefore, of prime consideration. A business may become distinctive as readily for its policy as for the character of the goods it handles. Within the policy of a business is included the entire scope of the relationship between the maker of the goods and the buyer of the goods, and between the handler of the goods and his customers.

Among the constituent problems involved in a consideration of a business policy are the house, or store, policy, the price policies, the problem of credit and discounts, and the general business practices. More specifically, there are the problems of a general price policy, of calculating percentage mark-up of price, of price maintenance, of credits and discounts, and of competitive practices. Besides these there are the subtler phases of human relationship, such as rules of courtesy, "store atmosphere," guarantee of goods, money refund on purchases, the development of personal relationship, and so on. These latter, however, are as much within the realm of psychology as of economics. A course in salesmanship would emphasize them.

**214. The House or Store Policy.**—Every store develops to a greater or less extent a code of practices. These deal with the employment relationship and the sales relationship.

They are a crystallization of the integrity and honest dealing of the management. The new policy introduced by John Wanamaker that the customer must be satisfied, or that of the house of Marshall Field which holds that "the customer is always right," illustrate the significance of a house policy.

As related to the selling question, the house, or store, policy becomes a merchandising policy. It directs the extension of credit to customers, the service items of delivery, rest-rooms, courtesy, inspection and return of goods, and so on. In it are involved economic considerations, psychological considerations and social considerations.

There is also an ethical phase to be considered in the establishing of business policies. There is the practical consideration as to whether or not the merchant is to put into practice the old adage that honesty is the best policy. In business, generally, a new word has been introduced into common usage for the purpose of expressing the new spirit that is entering business practice. This new word is "service" and includes a consideration of the merchant's duty to the community which he serves. In every social group, economic problems are tinctured with social problems. What the merchant gives in return for what he gets from the community is an important question. The mail-order house and many of the large retail establishments have won for themselves the reputation of unquestioned integrity. They have done this by dealing fairly with their customers and by being willing to correct all mistakes. To be known as a reliable firm is an important asset for the merchant.

As a part of the business policy, there is the question of offering a guarantee as to the quality and quantity of the commodities sold. This guarantee means that the dealer is willing to stand back of every claim and every description regarding the commodities which he handles. The introduction of a guarantee into merchandising is of considerable significance. It is reflected in the character of the goods which the merchant handles, and it is an addition to his responsibility. It affects inevitably, also, the methods of advertising and of "puffing" his goods. On the other hand, there is the element of human nature connected with the guarantee. It is possible, under such a policy, for the unscrupulous customer to take advantage of the merchant. The trend of experience on the guarantee of goods has been, however, that the customer responds readily to such methods of dealing.

The old principle underlying the buying and selling of goods, called *caveat emptor,* was that the buyer should beware lest the seller should deceive him as to the character of the goods. Under modern methods, this policy is disappearing. The consumer on the one side is losing his power of shrewd bargaining and his judgment of quality in regard to the goods which he buys. Very often, also, he buys the goods by samples or in packages and has no opportunity to inspect them. With the introduction of a guarantee policy, the old principle that the buyer should beware lest he be deceived is passing away. The two are essentially inconsistent.

Another asset which the merchant desires to secure is good will. This means that the customer returns again and again to make his purchases because he is satisfied with the treatment which he has received. The kind of goods sold and the kind of service offered in the selling are important factors in securing good will. On the whole, good will is the result of a successful store policy. Every merchant must work out for himself the most effective means of securing it.

**215. General Price Problem.**—The general price problem is primarily a problem of adjusting the conflicting interests. This is in essence the bargaining process. Buyers and sellers have come together with interests that oppose one another. The buyer seeks to find the best value for the most "reasonable" price, and the seller seeks to get the highest possible net return. The buyer often must purchase goods in the end, and the seller is under compulsion to set a price which will carry his goods off the shelves. It is under this process of adjusting business interests that a fair price is supposed to develop.

The question of price is related to every step in the distributive process. All parts of the distributive organization are said to exist because of a definite economic need. Where there is a definite service, therefore, there is also a fair claim for remuneration. The practical question is how much each service is worth in the medium of exchange. Obviously, this is a very complex problem. The manufacturer of a typewriter recently simplified the system of distributing his goods in such a way that he was able to reduce the price to the consumer from $100 to $51. Nevertheless, practically all the functions performed by the previous complex distributive organization were still necessary under the simplified organization. And yet it was possible to reduce the sales price by $49 and still maintain a margin for profit. There is also the question of special sales or bargain sales, in which the price is often greatly reduced. On the part of the purchaser, there are endless varieties of desires. The price, therefore, which the consumer is willing to pay will vary almost indefinitely. The general business theory, however, is that by means of the very operation of supply and demand working through the distributive system a reasonably fair price is determined.

Price is also connected with the theory of competition. It is supposed that under the system of fair competition, every price must tend toward a reasonable basis. It is by means of competition that supply is adjusted to demand and that the whole distributive system is made flexible. However inadequately this system may work in a given case, the general theory is still maintained that intelligent, open competition will adjust prices equitably.

The consumer has an interest in the price problem in addition to the mere fact that a price must be paid. It is to be remembered that if the margin of profit is too high, there may be a very material waste of social energy resulting. If too many merchants are called into the retail trade, the burden will fall upon the consumer in the form of retail prices. All instances of unfair price will tend also to derange the producing and distributing organization at the expense of the consumer. It may be that in some cases to-day the functions are too narrowly divided, so that more middlemen stand between the producer and the consumer than are necessary. This situation also falls at last upon the shoulders of the consumer. In general, uneconomic practices by producers and by middlemen will bring an added burden upon the consumer in the form of a high market price.

The price of commodities is also related directly to the cost of producing and distributing them. It may be said in general that the cost of producing and handling goods is the basis of prices. It is the basis, however, only in the sense that the price cannot go below such cost. There is also another problem related to cost. The question has often been asked: "Is it advisable to sell below cost, either temporarily for the purpose of advertising, or generally, by the individual, either manufacturer or merchant, who finds he is in an advantageous situation?" In other words, is it fair for every man, whether producer or dealer, to sell as low as he can and still secure a margin of profit? Certain department stores have declared that they do not dare to sell as cheaply as it is possible for them to sell, lest they drive out other competitors and thus suffer from the consumer's lack of opportunity to compare prices. A manufacturer of automobiles has refused to sell his machines as low as it was possible for him to sell them, lest he disrupt the entire automobile market. The whole problem is one of reasonable and fair adjustment.

The problem of price is obviously related to the problem of profits. This is on the theory that every one will do what pays him best, or what he thinks will pay him best. It is the opportunity of securing profits that directs the policy of manufacturers and merchants. The number of manufacturers, the number of wholesalers or retailers who engage in a certain line of business are in general directed to this business by profit opportunities.

In this connection, also, there is the question of "odd prices." This is largely a matter of psychology. It involves mainly the optical illusion secured by the odd figures given in the price. If a certain article is marked $1.99, the effect upon the mind of the prospective customer may be far different from what it would have been if the price were marked two dollars. There also is the consideration, largely psychological, as to whether or not prices should be shown. The mark-down sale and the advertising of prices have generally not been approved by the best merchants. There is almost always an element of suspicion connected with cut rates. It is difficult to convince the customer that he is getting the same grade of goods that has sold at standard prices.

There is the problem of standardizing prices. It is true, in general, that in a given market area there is a strong tendency toward a single price for any given commodity, modified only by the necessary charges for distributing and handling. Thus it has been shown that wheat, which sells at a world-market price, will have its price determined in the primary market and the local price will be established by a certain deduction from this primary-market price. The development within recent years of a great number of trade associations has greatly reënforced the tendency toward standard prices. Whether prices on the basis of grade should or should not be standardized under a system of so-called open competition is still an unsolved problem.

There is the consideration of price intervals. By this is meant the intervals or margins by which prices of the same commodities, though of different grades, are set. Take the case of neckties. Suppose a certain tie is priced at $1.50. It is the common practice to establish the next interval of price at least at $2. In the case of suits, the price margin between grades is much greater. The point is that these price margins are not set by careful calculation, but by standard practice and business habit. No customer without special or technical knowledge can determine whether the difference in grade is sufficient to cover the margin in price.

On the whole, the economic force which directs industrial and trade activity is the setting of price. The market price is the very core of commercial organization. The price itself is based upon market information. The forces directly affecting it are the most potent organizing forces in the market. Under a system of competition, it is believed that these forces in the long run work fairly for the producer, for the distributor, and for the consumer.

**216. Calculating Price Percentages.**—A practical problem arises in connection with determining not only what increase over cost-price should be made for selling-price, but also how the percentage should be calculated. The percentage is directly related both to the cost of commodities and to the value of the services performed. In general practice, there is a standard percentage that is used. This percentage is the basis of all mark-up of prices. There is here a difference in method, some merchants applying the percentage to cost price, and others to sales price in determining profits. The best practice is to figure the percentage on the selling, rather than on the cost, price. The determining of the margin which is a technical part of price setting calls for the best judgment of the merchant. "Each commodity, with the exception of branded articles which must be sold at a price fixed by the manufacturer, and articles of which the price is fixed by competition, should be examined and a price fixed according to what it will bring."[1] The whole problem is one for careful consideration and analysis.

**217. Maintained Prices.**—A problem related to business policy which has become of great importance within recent years is price maintenance. This involves the question as to whether or not the producer of goods shall retain the power of determining at what price they shall be sold by the retailer to the consumer. Presumably, these goods have been sold outright by the producer through the wholesaler, or directly, to the retailer. Title to the goods has passed from the producer. He has, however, advertised his goods to the consumer at a stipulated price.

This problem of price maintenance is a practical one of every-day business life which must be solved in the end by the business man himself. It is not by theory, nor by court decision, nor by precedent, nor by "fireside musings," nor by glances from a library window that this problem will meet a final satisfactory solution. There must be an overturning of opposing claims, there must be an array of facts to back up assertions, before there is victory for one side or the other. It seems very likely also that the elementary principle of priority of interest must first be established. Fixed price, like all business problems, is not a single or a simple problem. With it are combined the constituent problems of branded goods, of trade-marks and market control, of legal rights and commercial rights, of long-run policies and of business ethics, to say nothing of the overshadowing problem of social control. It divides itself, however, into two distinct parts; one has to do with the commercial phase of the problem, and the other with the legal phase.

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[1] Field, *Retail Buying*, p. 118.

218. *Commercial Phase.*—From the commercial point of view, the problem of price maintenance contains the issues of all business problems. These issues are of three different kinds; there are the issues of fact, the issues of economic theory, and the issues of business policy. In essence, the problem may be stated as follows: shall the producer of goods, whether identified or not, be responsible for quality and quantity and control the conditions of resale, or shall the distributor have the responsibility for quality and quantity and control the goods after they have passed from the hands of the producer? These questions should be answered either on the basis of public welfare, of business policy, or of legal reasoning. Shall the effects of the fixed resale price be judged from the point of view of business control, or shall they be judged from the point of view of competition? Satisfactory answers to these inquiries will afford a solution to this difficult problem. Much more data and analysis are yet needed, however, for a dependable conclusion.

The arguments made by those who favor price maintenance may be summarized as follows: the producer should have the right to fix the resale price of his goods, because (1) there is no other way to protect a living price for the dealer; (2) it is a helpful way of obtaining common-sense coöperation between producer and dealer; (3) it is necessary to maintain quality; (4) it protects the consumer from an excessive price; (5) it prevents unscrupulous dealers from using advertised goods as leaders; (6) the manufacturer has made his goods to be sold at a price; (7) it guarantees the goods to the consumer; (8) it prevents the deceitful, or fraudulent, cutting of price by the dealer; (9) it prevents dealers with large capital from driving certain goods off the shelves of small dealers by means of price cutting; (10) without fixed price, the dealer alone sets the price of goods for which he is not ultimately responsible; (11) real competition to-day is not one of price, but one between articles.

Those who oppose the fixing by the manufacturer of the resale price claim that the principle of price maintenance is not justifiable, because (1) it is selfish, in that the retailer desires to be protected from underselling by his competitors; (2) it is unfair, in that it prevents a merchant from giving his customers the advantage of his money-saving system; (3) manufacturers raise the price to pay for national advertising which is only more or less efficient; (4) it puts the big dealer on a plane with the small dealer; (5) it does not accomplish the desired results, namely, increased sales; (6) it enables imitators to sell at high prices; (7) the manufacturer attempts to control goods after he has transferred the risk for them; (8) it is not primarily any of the manufacturer's business; (9) as a principle, it is not in accord with the general proposition that a declining price means increased sales; (10) it is not proved that this policy either maintains or enhances quality; (11) standards of quality, in the great mass of goods, cannot be set; (12) the manufacturer and the dealer are interested parties, and a system of price fixing by interested parties is inadvisable; (13) the objection to price cutting is mainly an opposition to disturbers and invaders of the old system; (14) the fixed-price system stands in the way of experimenters.

This problem of the commercial effects of price maintenance must remain unsolved until there is further experiment with it, and until a sufficient basis of fact is established. To-day there are great numbers of manufacturers and merchants on both sides of the controversy. Obviously, however, a certain class, especially of retailers, are favored by such a practice. They are the small, incompetent retailers who are guaranteed a margin of profit which may permit them to meet the competition of their larger and more efficient competitors. These dealers are in favor of price maintenance. A bill has been before the Congress for several years to establish the legal status of fixing resale price. It has not yet, however, succeeded in being enacted.[2]

219. *Legal Phase.*—A number of cases have been tried by the court, based upon the right of the producer to fix the resale price of his goods. The great majority of these cases have been centered upon technical points of the law and not upon the general principles underlying this problem. The various points which have been developed in the cases at law are the legal rights in regard to secret processes, copyrights, patents, and licenses of sale. In all of these instances, however, final recourse has been had to the Sherman Anti-Trust Act. This means that the question has ultimately been one of monopoly, of restraint of trade, or of illegal combinations.

Instances of legal rights in relation to secret processes are to be found in the early cases such as Miles Medical Company *v.* Platt,[3] Hartman *v.* John D. Park and Sons Company.[4] The most noted case dealing with copyrights under the law is that of Bobbs, Merrill and Company *v.* Strauss.[5] The question of patent rights is dealt with in the case of Henry *v.* Dick,[6] and U. S. *v.* Kellogg's Toasted Cornflakes,[7] and Bauer *v.* O'Donnell.[8] The license of sale rights are discussed in the case of Victor Talking Machine Company *v.* R. H. Macy Company.[9]

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[2] Compare the Stephens Bill.

[3] 142 Fed. 606.

[4] 145 Fed. 358.

[5] 210 U. S. 339.

[6] 224 U. S. 26.

[7] 222 Fed. 725.

[8] 229 U. S. 1.

These cases are mostly beside the point of price maintenance. They have to do in general with common law rights as contrasted with statute rights. They have not settled definitely the relation of the principle of price maintenance to the Sherman Anti-Trust Law, nor have they discussed the relation of this principle to the new elements introduced by the Federal Trade Commission Act or the Clayton Bill.

There is one case, however, that is based upon the essential principle involved in fixing resale price. This is the case of the Fisher Flour Mills Company *v.* Swanson.[10] This is a decision of the lower court, and applies only to a limited area. The issue involved in the case is: has a manufacturer who has given a reputation to particular goods the right to fix in his contract of sale to retailers a reasonable minimum price at which the goods shall be sold? The decision in this instance declared that this method of sale did not come within the Anti-Trust Law, and that no patent rights were broken. It was necessary, therefore, to refer to common law in order to determine the principle involved. On this basis, it is declared that the fixing of resale price by this method is not against public policy. "The contracts fixing prices as incidental to some main contract and involving less than a controlling part of a given commodity in a given market, not proceeding from or tending to create or maintain a monopoly, will be sustained when the restriction is, under the circumstances of the particular case, reasonable in reference to the interests of the public and the parties." This contract was therefore declared valid and binding.

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[9] Sup. Rep., vol. xxxvii, p. 412.

[10] 137 Pac. Rep. 144.

The legal status of price maintenance is still not clearly determined.

It may be said in general that with respect to patented articles, their sale having once been accomplished, no right or royalty in the articles sold being retained by the patentee, and no profits from the sale shared by him, the resale price thereof cannot be limited or fixed either by notice attached to the article, or by contract. It must not be inferred from this that conditional sales whereby title is retained in the seller pending the performance of a condition, or transfer by license agreement, where such conditional sale or license transfer is for the purpose of maintaining price, would be tolerated by the federal courts. If there is any device by which a patentee or his assigns can legally maintain resale prices, it yet remains to be brought to the attention of the court.

To copy righted articles, the same general proposition applies as applies to patented goods.

With respect to proprietary medicines or trade-marked goods, where an outright sale of the goods is made, the manufacturer has parted with all proprietary right in the article and cannot therefore control the resale price of his product in the hands of the vendee.

The nearest approach to a successful indirect maintenance of price is by the method of withholding supplies of goods from those dealers who cut prices.[11]

**220. Problem of Credit.**—A part of the business policy of a merchant is the establishment of a principle to direct the granting of credit. Since the middle of the Nineteenth Century, the practice of extending credit and giving discounts for cash payment has had a great development. The small retailer situated far from the wholesale center and buying once or twice a year his allotment of goods needed to be financed while he sold them. This situation lies at the basis of the credit system which, in modified form, has come down to the present day.

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[11] Murchison, *Resale Price Maintenance*, p. 195.

In recent years, however, considerable attention has been given by progressive merchants to the problem of asking and granting credit. The retail dealer asks for credit only when he has not enough capital available to take advantage of cash discounts. As has been said, the large retailers with plenty of capital behind their operations can make a substantial profit on their investments solely through the discounts which they secure. It is, however, the problem of granting credit whether by wholesalers to retailers, or retailers to customers, that offers the greatest difficulty.

As regards the retailer, it can be said that the amount of credit to be given will depend on four chief considerations: character, ability, length of time, amount of capital. A man in business is "worth" exactly the cash value of his assets. His "credit" is measured by his power to borrow money and his ability to buy on time. Credit is no longer given as a favor to the borrower, but rather with a view to mutual profit. For the continued welfare, both of lender and of borrower, there is need of a careful examination of the retail accounts. It is also true that the terms of sale to retail customers will bear a definite relation to that same customer's terms of sale to others. Large wholesalers employ a man whose primary duty it is to make the necessary investigations for the establishment of a credit policy.

As has been said, the most enlightened credit policy will have to do with the personality of the individual. Credit can never be separated from character. The ability of a man to do business is also an important consideration. There is too the amount of capital actually owned by the retailer and invested in his business. Obviously a man with a large amount of his own capital involved will feel a keener and more direct responsibility for good business practice than a man who does not have so much at stake. It was estimated in 1915 that the number of failures in the country due to incompetence was 33 per cent, and the number of failures due to lack of capital was 23 per cent. How long the account is to run is another matter of great consequence. This will determine the amount of discount offered for cash sales and the item added to the price in order to cover interest on the capital represented by the goods sold on credit.

The problem of granting credit has become a special study in itself. All methods for discovering the necessary facts relating to the prospective borrower are used by the up-to-date credit man. He makes inquiry as to the previous relationship with the customer. He inquires into the books of the retailer. He appeals to the Credit Men's Association. He looks up the firm in Dunn and Bradstreet's. He asks the borrower to fill out certain blanks and by all possible direct and indirect methods, he tries to discover the essential facts upon which a sound credit policy can be based. In recent years also, the Federal Trade Commission has been doing excellent work in the matter of standardizing accounting systems so as to render possible for the retailer, as well as for the wholesaler who grants him credit, a more accurate knowledge of his business. A pamphlet recently issued by this Commission declares: "The small manufacturer, the country storekeeper, and the retail merchant often do not get at the banks the credit that they ought to receive, due to the fact that they are unable to present balance sheets in accordance with good business practice. These men, as a rule, are just as good business men, in many respects, as those of larger operations. They have brains, ability, knowledge of their wares and of their customers, but they do not speak the language of the banks, in that they are not able to present a statement showing their assets and liabilities."

The Credit Men's Association also has undertaken a nation-wide campaign of education for the purpose of educating the retailer to a better knowledge of his business. They are carrying on this campaign not from any unselfish motive, but in order that their own problems may be more easily solved. They state in a recent report that "as grantors of credit, we are vitally interested in bettering business and credit conditions. Any movement that makes it safer to transact business naturally receives our attention and support. It is, therefore, not surprising that the National Association of Credit Men, the personification of honesty and efficiency in business, should be tremendously concerned in the standard of business of the retail merchant."

The retailer has his credit problem in relation to the customer. How much credit should be granted to the customer, and for how long a time, are very critical problems, and of special importance in periods of radical change or of uncertainty. Many a retailer has been bankrupted because he has been too generous in granting credit. On the other hand, many department stores and other large dealers have a well-defined policy to encourage credit or charge accounts. They find that these bind to them the customers who buy on time. The retailers who grant credit to their customers must meet in competition the mail-order houses, the chain stores, and economy stores that have reduced the retail prices on goods by eliminating to a large extent credit and delivery service. The entire problem of granting credit to customers is one to be solved by the individual merchant in his own house policy.

**221. Unfair Competition.**—The formulating of business policies must inevitably involve the question of general business practices. With these is connected the problem of unfair competition. What is fair and what is unfair remains yet to be definitely determined, either by business men or by the courts. The task of defining unfair competition has been squarely facing the Supreme Court of the United States for several years. But that august body has not yet made a thorough survey, nor has it laid the foundation for an enduring and practical definition. Until it has done so, both practical business men and economists will remain uncertain.

Fair competition has been defined as economic competition on the basis of efficiency. Whatever practice cannot fulfill these conditions should be declared unfair. The points in production and distribution at which competition actually occurs are various. It may be due either to inequality in size, or access to raw materials, or location, or unusually capable workmen, or able management, or new machinery, or patents and special processes.

The Federal Trade Commission that was established to deal with this particular problem has indicated certain practices as being unfair. They are as follows: local price cutting; operation of bogus independent concerns; maintenance of "fighting brands"; lease, sale, purchase, or use of other articles as a condition to the lease, sale, purchase, or use of certain required articles; exclusive purchase and sales arrangements; rebates and preferential contracts; acquisition of exclusive or dominant control of machinery or goods used in the manufacturing processes; manipulation; black lists, and white lists; espionage and use of detectives; coercion, threats, and intimidation; and fixing the channels of trade. All of these methods will be judged largely from the point of view taken, and different conclusions may be reached, due to differences in attitude. The problem can be attacked either by establishing legislation to direct and limit business practice, or by the self-discipline of business men. Undoubtedly, the best and most enduring results would be obtained if unquestioned business practices developed from business itself and were not left to be enforced by outside influence.

Competition cannot be fair unless it is intelligent. More intelligent competition can only be secured by a better knowledge of business principles. Progress undoubtedly is being made toward better business practices. Many methods that only a few years ago were permitted are now wholely discarded. It is probably true that fairness in business practice is wholly relative, and that with an increasing knowledge there will be constantly a rising standard of practice.

A more thorough analysis of business practice should reveal the source of responsibility at every step in the economic process. When this responsibility is once definitely located, the problem of dealing with practices will be greatly simplified. There is a growing attitude on the part of business men to carry on their businesses openly and with a full knowledge on the part of consumers and competitors. Many retailers, wholesalers, and manufacturers to-day are declaring that they have nothing to conceal. Such an attitude of openness and frankness can arise only from a conviction of fair dealing; wherever such an attitude exists, unfair competition will be done away with.

**222. Price Cutting.**—The movement for standardized prices that has accompanied the standardization, trade marking, and advertising of goods, has been reënforced by the rapidly multiplying trade associations, and has been aimed at the stopping of price-cutting by retailers. Methods of reducing price are countless in number, but fall into two general groups: (1) direct price cutting, and (2) indirect price cutting. The first group is by far the larger and more varied. It is illustrated by the bargain sale and "leader." The second type is illustrated by the use of trading stamps and coupons.

The "new type" of retailer, such as the department store, the chain store, and the mail-order house, by buying in large lots seeks a substantial quantity discount and claims the right to pass this saving on to the consumer in a lowered retail price, in order to increase the volume of sales. The manufacturer, who has branded his goods and advertised them, wants to keep them on the shelves of the regular retailer and objects to price cutting by the big retailer. So likewise does the regular retailer. This contest underlies the whole problem of price maintenance.

Special sales, such as bargain sales, season-end sales, fire sales, mill-end sales, etc., are often used to move goods off the shelves of retailers or out of the factory. Even when legitimately used, they are a confession of error in judgment on the part of the buyer or the manufacturer. He has misjudged the market at the price asked. Such a system also is open to ready abuse. As a settled prearranged policy it is uneconomic. For the dealer, more frequent and smaller purchases with a speedier turnover is better business. For the manufacturer, a more careful study of the market and a more conservative production planning is better business.

The use of trading stamps or coupons is a question of policy. As a means of advertising, of drawing trade, and stimulating cash purchases, they are effective, as the violent opposition to them shows. The opponents claim that they are forced into using them against their will and desire. This is positive proof of their efficacy. Whether or not the very fact that such a policy, by one or more merchants, will drive others to the adoption of it, does not in the end stultify its effects, is a serious question. Like all other claims, this one can be substantiated only by experience.

The means used to abolish price cutting has been an appeal to the law. Decisions of courts and statutes are urged to prohibit price-cutting policies. Each side accuses the other of dishonesty. The manufacturer and the regular retailer declare that price cutters deliberately cash in on the goodwill attached to well-known brands for selfish purposes. The large retailers claim that manufacturers and old-line retailers are holding from the public a legitimate and realizable lower price. There may be truth on both sides. But the spirit of dishonesty is never destroyed by legislation. So long as competition runs on the basis of efficiency and fair dealing, there is no need for restrictive legislation.

## Suggestions for Study

The business policies connected with the commodity investigated by each student should be carefully studied at this point. The following topics can be taken up in the classroom discussion:

### *House or Store Policy*

1. The meaning of house or store policy.
2. A merchandising policy in its relation to selling function.
3. Economic, psychological, ethical, and social considerations in a business policy.
4. The guarantee policy.
5. The element of risk in a business policy.
6. *Caveat emptor* in modern business.
7. Goodwill and business policy.

### *The General Price Problem*

1. Economics of price.
2. Social aspects of the price problem.
3. Standardizing prices.
4. Psychology of "odd" prices.
5. Price intervals.

6. The fair price.
7. The normal price.

### *Price Maintenance*

1. Commercial importance of fixed resale price to large manufacturers, small manufacturers, wholesalers, retailers, consumers.
2. Maintained price and monopoly.
3. Maintained price and competition.
4. Maintained price and quality of goods.
5. Maintained price and advertising.
6. Trend of legal decisions.
7. Maintained price and copyrights, patent rights, secret processes, licenses of sales.
8. Maintained price and restraint of trade.
9. Legal principles *vs.* commercial interests.

### *Problem of Mercantile Credit*

1. Origin of problem.
2. Data for granting commercial credit.
    - (*a*) Kind of data needed.
    - (*b*) Sources of data.
3. Function of credit man.
4. Costs of granting credit.
5. Credit and competition.

### *Unfair Competition*

1. Theory of free competition.
2. Regulated competition in a democracy.
3. Enforced competition.
4. Point of view in judging competitive methods.

READINGS:

### *House or Store Policy*

Nystrom, *Retail Store Management,* Chap. XII.
*Store Management,* Chap. VII.
Swinney, *Merchandising,* Chaps. II, VII.

Johnson, *Business and the Man,* Chap. V.
Fiske, *Retail Selling,* Chap. III.

### *Price Policies*

Nystrom, *Economics of Retailing,* Chaps. XI, XV.
Cherington, *Advertising as a Business Force,* pp. 330-428.
Mahin, *Advertising,* Chap. 19.
Rogers, *Goodwill, Trade-Marks, etc.,* Chap. XXVII.
Fernley, *Price Maintenance,* Chaps. II, III.
Stevens, *Unfair Competition.*
Montague, *Business Competition and the Law.*
Murchison, *Resale Price Maintenance.*
*Annals of the American Academy of Political and Social Science,* January, 1916, p. 55.
*American Economic Review,* vol. vi, No. 1.
*Journal of Political Economy,* January, 1916, pp. 921-950.
*Printer's Ink,* April 2, 1914, p. 33, 64; April 23, 1914, p. 23; November 5, 1914, p. 51; March 19, 1914, p. 64; December 31, 1914, p. 52.
Cases: 142 Fed. Rep. 606; 145 Fed. Rep. 358; 149 Fed. Rep. 838; 214 U. S. 339; 220 U. S. 373; 224 U. S. 26; 222 Fed. Rep. 725; 229 U. S. 1; 137 Pac. Rep. 144; 227 Fed. Rep. 46; 227 Fed. Rep. 124; Sup. Rep. vol. xxxvii, p. 412.

# CHAPTER XVIII

## DEFENDING AND EXTENDING THE MARKET

**223. The Problems of Market Extension.**—There are two general problems facing any merchant in his relation to his market. One is a problem of defense, that is, to hold the customers already secured, to guard his good name, and to prevent other merchants from cashing in on his own efforts. The other is a problem of offense, that is, to extend the frontiers of his market or to sell more intensively in the territory already covered.

An attitude of defense is a passive one. Just as no military victory was ever gained without an attack, so no great commercial success will be achieved without an aggressive policy. Few manufacturers or merchants are satisfied with the present size of business, even in the abnormal prosperity of war times. The typical American manufacturer wants to tear down his factories and build greater ones, or at least to attach additions, and if his output now runs up into thousands, he desires millions; if into millions, he wants tens and hundreds of millions. And so likewise with merchants who seek greater business volume year by year.

Business experience and the romance of American business incite such ambitions. The home market for most products has had a natural and rapid growth, due, of course, to increase of population and of purchasing power, and to better general education and transportation facilities. But the market offered by our own 105,000,000 inhabitants is not big enough. There is a wideawake demand for a foreign market. The eyes of manufacturers and merchants are lifted to the far-distant horizons; men speak to-day casually of the South American market; orders are being sent to the Orient; a special corporation for fostering trade with Russia has been organized.

Thousands of business men, who do not yet look across the sea for more trade, are studying more minutely the nooks and corners of the home market. They want to sell more goods either at the expense of rivals' sales, or through increased purchases of consumers. In order to realize this ambition, their analysis turns upon new appeals, new motives, newly awakened desires, new types among the consumers, upon new forms, new packages, more attractive appearance, or better general adaptation of the goods, and upon the most effective methods for defending the good name and the goodwill of their products.

Problems, therefore, have arisen concerning trade names, trade-marks, the form and general appearance of the commodity units, and the most forceful selling points. In the solution of these problems, law and psychology are intermingled, and even art has its voice. Some attempt is here made to show how to discover new fields and new methods, and to define the defensive rights of the successful merchant.

**224. Scope and Character of Market.**—As has been shown, the character of a market is dependent to a great degree upon the character of the commodity. But a market may be either developed or undeveloped, either actual or potential. It may already be overdone; one would not, for example, invest large sums of money to-day in a national company to sell horsewhips. But the scope and character of the market will in turn largely determine the method used to reach it. This holds true for manufacturer, jobber, and retailer. The selling medium may be either salesmen, or advertising, or both.

In the selection of the medium, the scope and character of the market will be an important factor. Many forms of advertising are less expensive than salesmen. The volume of business may not justify a heavy expense. Whether sold through a salesman or by description, if the market is to be retained in a keen competitive struggle, and especially if it is to be extended, there must be a careful analysis of the commodity unit, and an assiduous building up of defenses through trade-marks and trade names.

Whether the market is to be more intensively cultivated or is to be more widely extended, a careful scrutiny must be made of the commodity as to the possibilities of appeal that it contains. Goods are made to satisfy human wants, and the practical problem of salesmanship is to mate the commodity and the want. An early step, therefore, in extending the market is a careful study of the most effective appeal.

**225. Analyzing the Appeal.**—Primarily, the analysis of appeal is a study in human nature; it is largely a matter of psychology. One successful salesman holds to the theory that the most effective appeal is by suggestion through repeated impressions. This is not so much a matter of persistent advertising as it is of putting things before the prospective customer so obviously that he cannot escape noticing them, and so persistently that finally he succumbs to suggestion and buys. Practically, this has meant the placing of as many hurdles as possible in the way of the prospective buyer who has entered the store.

This method, however shrewd it may be, is not a high type of merchandising. True salesmanship is profounder than this is more farseeing, for it works along the line of long-time policies. Real salesmanship is real service and not merely putting something over. The analysis of appeal is broadly economic in character; it is an analysis of utilities.

The best appeal is to human wants, real or potential, that make for better well-being. If true merchandising is service, if selling is making possible the satisfaction of wants that are justifiable and worthy, then the analysis of appeal is a study of a commodity in all of its relations to those wants. It is a study of a commodity that is philosophical and ethical as well as economic. Specifically, such an analysis may take any one of several different methods.

A constructive study of appeal calls for business imagination. It is in fact creative work in as real a sense as the work of the musician or painter. The best merchant, though not necessarily the most successful financially, is a leader in his community; his customers rely upon him, accept his judgment, follow his suggestions. If the merchant is all that he should be, he is a powerful factor in directing purchasing power.

The appeal may be studied by looking within the commodity or by looking within the people. It may be form, or appearance, or service, or use. One may inquire as to what feature about the goods, either their manufacture, appearance, quality, use, or price, will stimulate interest and create a desire for their possession. On the other hand, one may ask what means may be found for making specific appeals to individuals. Appeals for the "shawl" trade will differ from those for the limousine trade.

**226. Appearance of Commodity Unit.**—An early consideration of the commodity whose market is to be extended is the appearance that it makes. It is possible to transfer a commodity from the staple class to the specialty class of goods by attention to its appearance. A tooth brush, for instance, may be sold from an indiscriminate group lying on a counter, or it may be wrapped individually in a paper envelope. A premium can be charged for this simple service of giving individuality to a staple commodity. A loaf of bread can be sold either wrapped carefully in paper or exposed to the elements. In the one case, the loaf may never be touched by human hands, and will look clean and sanitary. There are many other such little touches which will give distinction to a commodity unit without material expense on the part of the dealer. In fact, there is here a whole realm of psychological facts in the matter of taste which may be carefully studied.

In a study of the commodity unit, there will always be certain practical considerations. Not only is it the duty of the manufacturer and merchant to analyze his goods with particular reference to the human wants which they are intended to satisfy, but also to consider the matter of convenience of size. There are certain manufacturers of macaroni who have had a difficult problem to meet. This commodity had been sold in a standard package for a price which was printed on the outside. The rising costs of materials required that a change should be made. As has been pointed out, it was possible for them either to put less material into the box, or to increase the size of the box and the price in proportion to requirements, or to increase the price outright. Consideration, however, had already been given to the amount of macaroni which the average family would be likely to buy. In the original package, this amount had been nicely adjusted to the average family requirements. Any change in amount would therefore disturb this adjustment. Wheat flour is usually sold on the basis of a barrel, which is supposed to contain 196 pounds. In the large cities where storage space is greatly limited, such a large unit is impracticable. Dealers have therefore insisted that smaller units should be used. In certain times of fluctuating prices, flour has been sold, by such retailers as chain stores, by the pound. In many instances, one-eighth of a barrel, or even one-twelfth of a barrel has been put up in separate packages. Sugar is another staple now found in packages as small as one-half pound. The basis of this entire problem of adjusting size of a purchasable unit to the convenience of customers is to enable them to buy what they want in the amount they want. This is, of course, a part of the duty of the retailer.

Another consideration in studying the commodity unit is the matter of standardization. It is obviously possible for a manufacturer to standardize both the quantity and the quality of his products. If the manufacturer has not done this, it remains possible for some middleman to perform this function. Standardization, however, must be done before the moment of sale. It is a matter of preplanning. Manufacturers and dealers have not been slow to see the possibilities for control which lie in the standardizing of a commodity. The maker, for instance, can determine a standard unit for his goods and, either through advertising on the package itself or through some other medium, can compel his dealers to adopt this unit. It is interesting to note that the growers of citrus fruits have attempted by such means to control their commodities until they reach the hands of the consumers. Oranges and lemons are wrapped in tissue paper after having been carefully graded by special processes, and these wrappers presumably protect the consumer and the grower from all unscrupulous dealers. In fact, standardization of quality and quantity is so potent a force as to compel fair dealing on the part of the middlemen.

It is obvious, however, that if commodities leave the hands of the maker unstandardized either as to quantity or quality, there is opportunity for some middleman to control the marketing process by means of the standardization. Some large jobbers are to-day doing this for a number of staple commodities. The particular point to be emphasized is that whoever standardizes the goods is in a position to control their distribution.

The most perplexing problem in connection with standardizing commodities has to do with those goods that have a large element of style in them. During the stress of the war, the Commercial Economy Board in the Council of National Defense undertook to set different standards for the making of shoes. These standards had to do with the height of shoes, the character of the heel, and the quality and kind of material which went into them. It was recommended, for instance, by this Board, that for the fall season of 1918 no women's shoes should exceed nine inches in height, measured from the breast of the heel at one side of the center to the top at the side of the finished shoe; that no children's or misses' shoes should exceed seven inches in height; that all men's shoes, except canvas, should be restricted in color to black and two shades of tan; that no women's shoes should be of colors other than white, black, two shades of tan, and two of gray.

In foreign countries, the governments have on occasion undertaken to standardize the styles in wearing apparel. It is said that the British Government was unable to sell a great many of the standard suits which it had made for men. The point to be noticed particularly is that the will of the customer may revolt against the standard established by the producer.

A further consideration of the commodity unit has to do with placing the material in a package. There are obviously several advantages, especially from the point of view of the manufacturer, in placing products in standard packages. The package itself offers certain advertising possibilities. It protects the goods against misuse of the good-will of the producer by competitors. It protects the goods against unscrupulous dealers. It also protects them against abusive and unsanitary conditions and methods of handling. It enables the producer to indicate to the consumer in writing, even over his own signature, the quality and quantity and to indicate what in his judgment is a fair retail price. Goods that have been placed in neat, convenient, standard packages can usually be handled more readily than goods that are sold in bulk. It is even possible to add certain by-products of service by placing the commodity in such a container as may later on be used in various ways by the consumer. There is, for example, the familiar story of the can containing oil which has served many a useful purpose in far-away places of the earth. It is also easy to identify goods which have been placed in packages. In many cases, the package itself has given a personal touch to the commodity.

One manufacturer of piston rings has declared that the package that contains his special product affords the consumer protection in five different ways. "It is your protection against substitution; it protects the garage and repair man from having palmed off on him inefficient imitation rings; it protects the rings themselves from rust and the effects of rough handling while in stock; it identifies the goods as being our own make; it protects you in the matter of price." For all of these services, however, the consumer must pay. Package goods undoubtedly carry a higher price in the market than goods that are sold in bulk.

It may be pointed out, in this connection, that packages serve a further purpose. As a matter of fact, the placing of a commodity in storage in small units is accomplished by the use of protecting containers. Like the snail, the commodity in a package carries its shelter along with it.

There are difficulties, also, connected with the placing of goods in containers. In the first place, it is not possible for purchasers to inspect them. They are compelled to buy "sight unseen." The consumer, therefore, may find after he has made the purchase that the commodity is not what he thought it would be. Once an error of this kind is made, the experience is always associated with any given package. The producer has, in consequence, a difficult problem to overcome in restoring the good name of his product. It is also hard to change either the quality or the quantity or the price once these have been established in connection with a standard package. Commodities that are placed in containers, as has been said, have an added cost for this added service. And they must meet the competition in the market of goods sold in bulk. In times of high prices, competition of this kind becomes very severe.

On the whole, however, there is a very decided tendency in the United States toward placing goods in containers. This method has been found extremely useful by manufacturers who plan to control the marketing process of their commodities. Undoubtedly, also, a better quality of goods is being marketed to-day in packages than formerly was sold in bulk. Either as a result of standardizing and identifying commodities by means of packages, or along with the development of packages, there has been a general toning-up in the quality of goods. There is also the æsthetic side to be considered in regard to package goods. In most cases, it is possible to make the package far more attractive than the commodity itself can be made. On the other hand, there are some instances where a commodity has special value for display. This is the case with citrus fruit. Some commodities are angular and awkard-looking in themselves and need to be put in neat, snug containers. This often adds greatly to the advertising effect in the eyes of the consumer.

**227. Identification of Commodity.**—The best weapon that has been developed in modern merchandising, both for defense and for offense, is identification. This means that the name of the maker and the source of the commodity are known to the consumer. Obviously identification carries along with it certain responsibilities. A manufacturer who identifies the goods which he makes is no longer an anonymous producer. Although he may be located thousands of miles away from the ultimate consumer, it is possible readily and directly to hold him responsible for all defects either in quantity or in quality. Ultimately, the one who identifies a commodity, whether producer or middleman, undertakes the responsibility either of good will or of ill will.

On the other hand, the identification of commodities enables the producer and the jobber to sell their own products at long range. The sale may be consummated either by description in a letter or through general advertising. In all national advertising campaigns in this country, identification of commodities is essential.

Identification also secures to a large extent the control over the distributive process by the one who identifies the commodity. In fact, identification is the most powerful influence in modern merchandising. It has made the names of certain commodities household words from one end of the country to the other. It has announced to millions of consumers the policy of honesty and integrity of certain great producers. It influences the buying habits of millions of consumers. Retailers have been compelled to carry the identified commodities. It underlies the whole system of advertising.

These two policies of modern business, standardization and identification, have made possible the large-scale production for which the United States is known throughout the world. The repetitive processes required for the manufacture of standard goods have called for the wonderful development of machinery during the past fifty years. Under standardization, output has been immensely increased. The identification of products which have been turned out by means of standard processes has put into the hands of the large producers a practical, controlling influence in the marketing of many commodities. From these two things, standardization and identification, all modern marketing methods flow.

Goods may be identified either by producer, by wholesaler, or by retailer. As has been pointed out, here lies the tremendous struggle between the large manufacturers, the large jobbers, and the large retailers. Each one desires to identify the product which he handles. It is not possible for all of them or for any two of them to identify the same product. They already realize, however, the unlimited possibilities for control which lie in identification. The manufacturer understands that if his name is not attached to the goods he makes, he is an anonymous producer, and that some middleman stands between him and the consumer. The jobber realizes that a large part of his power is gone if he handles only those commodities which some one else has identified. The retailer has discovered that his importance is diminished if the goods which he handles are identified by producer or jobber. Out of this clash of interests has grown much of the chaos in the distributive process of to-day.

In general, goods may be identified in either one of two ways; it is possible also to use both of these methods. One is to place on the goods a trade name. The other method is to place a trade-mark on the commodity. Frequently, to-day, both a trade name and a trade-mark will be found on identified package goods.

**228. Trade Names.**—There is no clear-cut distinction between trade names and trade-marks, because a trade name may serve the function of a trade-mark. It is, nevertheless, true that certain trade names are used purely for the purpose of identification, and that in addition to the name a certain marketing symbol is used. The object in placing a trade name upon the commodity is usually to attract the consumer's good will for the commodity to the one who has identified it with a trade name. Thus, a manufacturer may place his trade name on a commodity and the consumer will connect the producer's name with the goods he has bought. If the jobber and the retailer place a name upon goods, then the consumer will connect them with the commodity.

Many kinds of trade names are being used in business to-day. They have been derived from several different sources. It may be, for instance, the name of the firm itself that is placed on the commodity. In other cases, proper names and names of places have been used as trade names. In some cases there has been a shortening of a long name, or the combining of syllables for the making of a unique and attractive trade name. A common method in vogue some years ago was to construct a diminutive form of the name of the commodity itself. For example, "Wheatlet," "Leatherette," and many other such names were formed in this way. Occasionally, compound words have been made up to serve as trade names, such, for example, as "Palmolive," "Walkover," "Spearmint," "Meadowgold." For the purpose of attracting attention, there have been deliberate misspellings of words, as "Shure-on," "Uneeda," "Noxall," "E. Z. Seal." Other devices to secure a unique and attractive trade name have been used, such as the initials of the firm, or the construction of a word that has no meaning, or the blending of names. The only limit to the sorts of trade names is the imagination and the ingenuity of the business man.

There is a legal phase to consider in connection with trade names. The law has stipulated certain rights to use and to defend such names. For instance, it has declared that a man's name is his own and cannot be used without his consent. Neither is it lawful to use a name for the purpose of injuring some one else. The situation arises on occasion where two producers have the same name. If one has already established his name in connection with his goods, it is not permissible for the second to steal away his goodwill. On the other hand, the law recognizes that every man has a right to use his own name in his business. He must not, however, use that name fraudulently. In every case, it is a question of fraud that should decide, that is fundamental.

It is furthermore granted that a man has the right to describe the goods which he sells. A dealer is not permitted, therefore, to adopt a descriptive adjective as his trade name for the purpose of preventing others from using it. It is even possible for such a word as a descriptive adjective to take on a meaning so unique as to permit of its being used by a business man as a trade name and defended against all competitors. Where such descriptive words have been used as trade names, however, the law does not allow a rival to use the same words for the purpose of deception. The burden of proof in such an instance is upon the one who uses the word as a trade name. He must show that this particular word has lost its descriptive significance and has taken a well-recognized designative significance. An instance of a word that fulfills these requirements is to be found in "Holeproof."

**229. Trade-Marks.**—As generally defined, a trade-mark is a word, letter, device, or symbol or combination of these used in connection with merchandising and either inherently or by association pointing distinctly to the origin or ownership of an article to which it is applied. It has been found a convenient way of disclosing commercial source, or origin, of goods that are sold in trade. Practically, a trade-mark is a symbol of business goodwill. It is therefore not possible to separate it from the goodwill which it represents, and that good-will in its turn cannot be separated from the business to which it is attached. It follows, therefore, that a trade-mark is inseparable from a business.

The trade-mark, however, must be distinguished from a copyright or a patent. A copyright gives the exclusive right to multiply copies of a published intellectual work. A patent "is the exclusive right to make, use, and vend any new and useful art, machine, manufacture, or composition of matter." Both copyrights and patent rights exist only by power of statute; also they depend upon the creation or invention of something new. The right to a trade-mark, on the other hand, is not statutory, but is wholly a right of common law, or as modified by the laws of the State. The right to a trade-mark is acquired only by priority of adoption, coupled with the actual use of the goods in the market. To acquire such rights, the use of a trade-mark need not be extensive. It is enough if goods bearing the trade-mark are on sale in the market. The use of or the opportunity to use a trade-marked commodity, however, must be continuous and not merely casual and occasional.

Since a trade-mark has for its purpose the indication of the commercial origin of a product, there are certain requirements for its validity. Names that are purely descriptive are not valid trade-marks unless they have taken on a peculiar and generally accepted significance. Geographical names, likewise, cannot be used as trade-marks because the right to use them cannot be denied to the public. The same criticism holds for the use of personal names. If the trade-mark itself is deceptive or untrue, it is not valid. It is not permissible to use either the national flag, or that of any state or municipality, or the seal of the national Red Cross, or of any fraternal organization, or anything obscene or immoral, as a trade-mark. The one exception to this principle is that the law permits the use of trade-marks that were established before the year 1905.

Valid trade-marks should have the following characteristics: they should be affixed, branded, or impressed upon the article or package; they should be arbitrary in character, and not deceptive; they must be used in lawful trade; they must be of such a character as to make it possible for the public to distinguish the article from those of all other makers or dealers. The courts have not yet decided whether it is valid for merchants to use the same name on different kinds of articles. The courts have held that identical trade-marks should not be used on goods of such similar character as to afford an unfair use of established good-will, or as to cast any doubt upon the origin of the goods. All trade-marks should be duly registered, but registration is not in itself positive proof of a right to use a trade-mark. That right rests solely upon the fact of priority of use.

It is possible to buy and sell trade-marks, just as it is possible to buy and sell the good-will of an establishment. In fact, certain trade-marks have been estimated as being worth millions of dollars. The American Tobacco Company, for instance, claimed that its trade-marks were worth $45,000,000 out of a total valuation of $227,000,000 for the entire plant. Other well-established trade-marks have been held to be worth a million dollars per letter. A certain manufacturer of soft drinks has estimated the value of his trade-mark at $5,000,000.

The legality and the effectiveness of a trade-mark should both be considered from the point of view of the consumer. The point of legality is decided by consideration of whether or not there is actually any deception to a reasonably careful man. For effectiveness, a trade-mark must be simple, easy to pronounce, readily remembered, and sufficiently suggestive to catch attention.

The number of trade-marks is rapidly increasing. During the year 1911, there were 7,000 registrations of trade-marks. Twelve thousand were pending at that time. Applications at the rate of 600 per month have been made for registration. Generally from 80 per cent to 85 per cent of the applications are granted. It has been suggested that there should be a national trade-mark established for the United States. This suggestion has been approved by the National Association of Manufacturers, who have adopted at a recent convention a resolution urging the establishment of a national trade-mark, such as "Made in U. S. A." The purpose in having a national trade-mark is to prevent the so-called legalized piracy of private trade-marks in foreign markets. The most common law to be found in foreign markets is one which holds that the fact of registration or prior registration establishes absolute right to a trade-mark. Many instances have been known where trade-marks that were established in the United States have been registered by citizens in foreign markets, thus preventing the sale of these well-known commodities except through special dealers or by the purchase of one's own trade-mark rights at a high price. It is wise for every business man to register his trade-mark both in the domestic and in the foreign market.

**230. Plant or Store as Appeal Asset.**—There are possibilities of appeal not only in the goods themselves, but also in the plant where they are made and in the store where they are sold. Manufacturers and merchants in the United Sates have only recently awakened to the possibilities lying in the attractiveness of the plant or store as an aid in selling products. It has been said that the one American contribution to architecture has been the skyscraper. There are, however, many manufacturing plants throughout the country that are most attractive in appearance and in location. Some of these have been made into show places for all the tourists who pass their way.

Probably the best example of the effectiveness of appeal through the plant where business is done, is the bank. There is an impression given, consciously or unconsciously, that the bank itself carries on safe and sound business in a substantial building. It is for this reason that one finds a magnificent Greek temple in the business center of some of our largest cities. There is no other justification for the great expense in such an otherwise unproductive structure.

Not only are there possibilities of appeal in the character of the plant or store, but also in the location of each. As far as a store is concerned, the principal considerations of location have to do with (1) the accessibility of goods; (2) the mass psychology in the movement of crowds; (3) the social class distinctions; (4) the business environments. Accessibility of goods is the most important consideration. A great mass of buyers make their purchases at the most accessible place. There is therefore to be considered the relation of the location to highways of traffic, the character of the passers-by, the display possibilities, the largest amount of natural light, and many other minor factors. From first to last, the prime consideration is a possibility of profit. The volume of trade and the expenses of operation, including the rent, are the essential items to be analyzed.

The problem of location is not the same for the manufacturer as for the jobber or retailer. Each must meet his own problems in his own way. The manufacturer can have his sales organization attached to his manufacturing plant, or established in some trade center. The jobber needs to have his plant accessible from the point of view both of the producer and of the retailer. The retailer must study the customer. This last is an endless problem. It includes the buying power of the people and customs of the people, the character of the local customers, the buying habits, the rents, the corner location, the best side of the street, and many more. All of these factors will have a different importance as they are related either to convenience goods, emergency goods, or shopping lines.

**231. Potential Markets.**—As has been said, markets are both actual and potential. For a merchant to hold the market which he now has, is a question of defense. The problem of increasing sales, of reaching new markets, is one of offense. Standard goods that are identified by trade names or trade-marks can be used in both defense and offense. The extension of a market, however, either intensively or extensively, requires a careful analysis of buying habits and purchasing power. A recent investigation into buying habits that was made by a large newspaper contains the following statement: "The merchandising service of this newspaper is able to put its fingers on the 101 items of knowledge that determine why people buy and why they don't." Knowledge of this sort is absolutely essential in laying out plans for extending the market.

Before a plan is made for reaching out into new territory or for developing the territory already covered, a careful analysis should be made of the possibilities for such extension. An investigation was recently made by the research department of a large publishing house as to the potential market for farm tractors. It was assumed that no farm of less than 100 acres could afford a farm tractor. It was found from the last census report that there were a certain number of farms in the country containing from 100 acres to 174 acres. There was another division of farms including all those of 175 acres and above. It was further found that the first group made up 24 per cent of the farms in the country. The latter group included 18 per cent of the total number. It was then assumed that one out of every five of the first group of farms afforded a potential sale and that three out of every five in the latter group afforded opportunities. A calculation was also made as to the number of farms that could support two tractors.

It was concluded that the total of these three groups constituted the entire possible market in the United States for the tractor. Figures were then found as to the number of tractors that had been sold. The final step was easy in determining the extent of the potential market.

A careful analysis of this sort is essential for the planning of any extension of market. It is possible, however, to secure data upon which a safe policy may be based.

## Suggestions for Study

The student should at this point analyze the possibilities for extending the market of the commodity which he has under special investigation. The following subjects will serve for class discussion:

### *Finding the Selling Points*

1. Selling points and business imagination.
2. Selling points and business analysis.
3. Selling points and creative work.
4. Selling points and business integrity.
5. Selling points as related to the consumer.
6. After all, what are selling points?

### *The Appearance of the Commodity Unit*

1. A critical examination of the commodity unit.
2. Commercial considerations connected with the unit.
3. Protection against competitors.
4. The commodity unit as related to the identification of goods.
5. Packages and advertising possibilities.
6. The commodity unit and "service."
7. The "new idea" in packages.
8. The commodity unit as modified by character of goods, by consumer demand, and by price.
9. Standardizing the commodity.

### *Trade Names*

1. The origin of the trade name.
2. The commercial function of the trade name.
3. Legal rights to use trade names.
4. Limitations to use of trade names.
5. The trade name and good-will.
6. Things to be considered in selecting the trade name.
7. Advertising value of a trade name.

### *Trade-Marks*

1. Trade-marks. *vs.* trade names.
2. Origin and development of trade-marks.
3. Trade-marks and distributive problems.
4. Registered trade-marks.
5. Trade-mark restrictions.
6. Trade-mark infringements.
7. Trade-marks and the consumer.
8. Trade-marks and the fixed price problems.

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# CHAPTER XIX

## THE SALES ORGANIZATION

**232. The Importance of a Sales Organization.**—For the manufacturer, the wholesaler, and the retailer there is a sales problem, essentially the same in character, but differing in the more superficial aspects. The manufacturer wants to reach, or at least to meet, the middleman who is to handle his goods, or the consumer who is to use them, or both. It must be remembered that the beginning and the end of every manufacturing activity practically is a merchandising problem; the manufacturer must buy and the manufacturer must sell. There is for him a problem of sales management and sales organization. The wholesaler likewise must have his sales organization, as well as his purchasing department. For the retailer, the sales organization is one of his chief concerns.

No matter how individual the problems of a given establishment may be, through them all runs a common element of human psychology. In the problem of labor management, the human element very largely predominates. With the merchant, there is the task of selecting men to go out and represent his business to the world. Within the establishment, there is the sales force that meets the customers as representatives of the house. This is a highly important task. It is largely a matter of temperament with which the merchant has to deal. The generalization is probably accurate that salesmen are more temperamental than mechanics or the clerks in an office. This fact complicates the problem of selection.

In every mercantile establishment of size, therefore, there is a house or store policy. This means, as has been said, the individual way of doing business. That is, the terms to be offered to a customer, the means to create a good name for the house, and the general method of dealing with customers. Whatever this policy may be, it is carried out in actual practice through the sales force. There is, therefore, a distinct need for training the sales force adequately.

Every business house of consequence is like a machine in that it must have its parts fitly joined together. They must be coördinated. The business must be well balanced. In this fact lies the need for organizing the sales force. The merchant, who has been financier and diplomat, must now become a sales manager.

**233. The Sales Manager.**—Somewhere in the selling process there must be a human factor, a salesman. Even a mail-order house must have its sales organization. The function of sales management, therefore, is essential, and some one must perform the service of a sales manager. Where selling is done at long range, by mail or by advertising, an advertising manager appears. As an establishment increases in size, there come to be distinguished four separate functions, that of the production manager, that of the finance manager, that of the sales manager, and that of the administrator. Of these four managers, the sales manager faces directly the selling problem.

The selling problem for the sales manager will be conditioned by the management's policies, by the character of the commodity, by financial considerations and by the general sales plan. Whatever the manager does must be in accordance with the house policy. In case the commodity is in universal, or at least widespread, demand, the problem is one of organizing for detail of operations and the best use of time. When the consumer must be instructed or the territory is to be sold intensively, the problem is one of technique and *finesse*, of care as to detail.

The sales manager works through the sales organization, which may be made up of an advertising department, an internal sales force, and a traveling sales force. He has, in consequence, the task of organizing and administering, of selecting salesmen, of training salesmen, and of generally coördinating the selling forces. Where complete organization is possible, it has been suggested that the sales organization should be divided into a personnel department, an advertising department, a sales-promotion department, and a recording department.

**234. Personnel Department.**—The personnel department in mercantile establishments, as well as in industrial establishments, is a new development. The term is a borrowed one used to cover many different activities. From a general point of view, however, these activities are all concerned with a certain definite function. This function is to select, train, educate, and dismiss the sales force. Only a comparatively large business can afford to establish a personnel department. In smaller concerns, its functions must be performed in connection with others. A distinct department of this sort marks a high degree of specialization in function. The specific problems with which a personnel department deals are selecting the sales force, training salesmen, holding sales conventions, and disciplining and dismissing salesmen. Each of these separate functions will be discussed individually.

**235. Selecting the Sales Force.**—The selection of employees in both commercial and industrial establishments is fast becoming a profession in itself. Since it is fundamentally a matter of human relationship, the science of psychology has been of great assistance. There are, for instance, certain psychological tests which are made of all applicants for positions. Naturally, these tests will differ in character for the selection of salesmen from those used in the selection of a working force in a factory. Some tests that are applied in the selection of salesmen are those of manners, appearance, indications of intelligence, good breeding, neatness and attractiveness of dress, and certain observation tests as to the action of the applicant during the interview. These tests vary with the establishments and the types of management. As a matter of fact, there is no limit to the tests that can be made. Whatever makes up the composite of personal impression will be used consciously or unconsciously in selecting salesmen. The stories that were written years ago of well-dressed office boys who secured jobs in competition with others and later became presidents or general managers have become out of date. To-day, the method is to apply scientific principles to this difficult task. The management usually requires every applicant to state his previous training and experience, as well as to give references to reliable men who can speak authoritatively about him.

In selecting salesmen, there are in general two main problems. There is the task of securing a competent, efficient inside force. These are the salesmen in the store. They will differ in type and possibly in training from those who meet prospective customers outside the store. In many respects, the selection of a sales force within the establishment is a distinct problem in itself. The other phase of the selection problem is the traveling salesmen. This type, which has developed along the lines peculiar to the United States, has come into existence since the period of the Civil War. The wholesalers found it necessary because of competition to send out representatives who traveled from place to place and took orders from the retailers. This type of salesman has continued to the present time. The outside force may be drawn from the inside force, the previous training of the men having taken place within the store. In no case is the traveling salesman competent to carry on his task until he knows the house policy and the problems inside the establishment. Even more than the salesman in the store, the traveling salesman is the personal representative of the business. His activities cannot be controlled by the management. He must be left largely to his own discretion. Decisions must be made by him without consultation. What he does and what he says is largely on his own initiative. This fact makes the selection of traveling salesmen a very important one.

**236. Training the Sales Force.**—The training of salesmen is also a recent development. It has generally been considered that anybody can go into business with practically equal prospects of success. No hurdles, such as special training, examinations, licenses, or diplomas, have been put in the way of salesmen, as is true of most professions. In fact, salesmanship has not been a profession in the past. To-day, however, more and more training is required of the successful salesman. This training may be given either by the establishment itself or by outside agencies.

Many stores require a period of apprenticeship before a salesman is considered a member of the sales force. Even to take care of the Christmas trade, most large stores will require that the extra salespeople shall pass through a brief apprenticeship of training. Usually this training consists of instructions in the use of various blanks and the sales forms, in special sales methods of the various departments, and in a demonstration of how sales are made. There are also some simple tests in arithmetic, and various instructions as to personal appearance, ways of meeting customers, and general deportment. Classes are sometimes organized in larger stores for the study of salesmanship problems. There are department stores that offer consecutive courses in training for salesmanship. These stores have a special room fitted up to be used as a class room, with a library in connection with it and a librarian-teacher in charge. The younger members of the force, the apprentices, and others who are ambitious to become more proficient are invited to join these classes.

The subject matter of the training given by the establishment itself is varied in character. In general, it will have to do with the policy of the house, a knowledge of merchandising and a stimulation of interest in the goods, certain technical knowledge of materials and manufacturing, and special instruction in methods of making sales. Part of the course will usually deal with distinctively departmental training. There is, for instance, the subject of home-decorating for salesmen in the departments handling pictures, rugs, wall-paper, furniture, and so ou. Some knowledge of good taste or harmonious colors, of the latest designs, and of the most popular fashions, will be imparted.

There is another phase of training for the salesman that deals with the problem of meeting the customers. In general, this training consists of ways of being useful to the customer in suggesting or advising as to what should be bought. There is, or should be, an insistence upon accuracy of statement and of honesty in dealing with customers. As the movement for training salesmen develops, the old-time tricks of the trade are being discredited. Earlier methods of leading the customer on, methods of managing him and securing his consent are no longer taught. Much is said, however, about the subject of reading character. Different customers must be dealt with in different ways. This is not only true in the matter of salesmanship, but also in every other kind of human contact. And knowledge of character, of ways of pleasing, and of lubricating all human contact are desirable both in the matter of salesmanship and in general intercourse.

The training of salesmen also is placing the emphasis upon the need of knowing the business. There are technical matters that are connected with every kind of business which should be learned thoroughly. There is need also that the salesman should analyze the merchandise which he sells in its relation to human wants. The salesman needs, moreover, a knowledge of economic principles. He needs a broad education so that he may understand more thoroughly the services which he is to perform. It is a part of the salesman's duty to educate the customers to new wants. He should be taught in his preliminary training how this may be done.

There have developed in recent years methods of making sales which are generally called sales talks. Several writers on this subject claim it is possible to teach the salesman a standard sales talk which he can apply on all occasions in selling the merchandise that he handles. It is obviously a superficial and parrot-like method of training salesmen. A far better way is to teach the salesman how to meet situations, how to use the information that he possesses under all circumstances. Sales cannot and should not be made wholly by the book. Human contact cannot be standardized. No engineer can be taught in the engineering school a standard practice for all the problems which he is to meet. The same is true of the salesman. Independent thinking, independence of action, honesty and integrity of character, and thorough knowledge of merchandise are much more important equipment than any standard sales talk.

The business colleges, which began to develop in the United Stacs just prior to the middle of the last century, for the purpose of applying mechanical devices to the office tasks in rapidly-growing establishments, later extended their courses to include salesmanship. Beginning with typewriting and stenography, they broadened their instruction to include business arithmetic, spelling, and punctuation, and a study of the selling problem. Many courses in salesmanship are now offered throughout the country by these institutions.

In the public schools and especially in the high schools, the demand for training in salesmanship has been reflected by the installing of such courses. The subject matter of most of these has to do with appearance, deportment, methods of making sales. As the subject has been studied, however, the instruction has become better, and a deeper knowledge has been made possible. The real question behind this offering of salesmanship courses in public schools is whether or not the burden for training apprentices should thus be placed upon the public.

The same movement for business training has been reflected in courses offered by colleges and universities. The past few years have seen the development of many schools of business administration in the universities of the country. In these schools, there are courses devoted to the subject of salesmanship. Generally, however, it is recognized that salesmanship is a broader problem than merely a matter of making a sale. It should become a profession in itself. Many subjects need to be studied. The most fundamental of these is undoubtedly the principles of economics. The course should include also subjects in marketing, in business correspondence, in psychology, in accounting, and many other allied subjects.

Often special courses are offered by companies that expect to sell their product direct from the factory to the consumer, to the young men and women who have a long summer vacation which they desire to make profitable. These courses consist very largely of standard sales talks and deal particularly with the commodity or line of goods which the company has for sale. The training very naturally is superficial. The personnel, however, which such companies secure from the colleges and high schools is of a quality much above the average, and many companies have found this method extremely successful.

**237. Holding Sales Conventions.**—Sales conventions are frequently held for the discussion of problems common to salesmen. These are largely the result of an organization of salesmen who have mutual interests. The purpose is to discuss the many problems which they have in common, and to make of the convention a kind of experience meeting. The social element is a large factor in these conventions. The salesmen often come back from them with many new ideas. The speakers are largely men who have achieved success. There are better efforts on the part of the salesmen as a result of the spirit of emulation which is assimilated at these conventions.

**238. Disciplining the Sales Force.**—It is necessary for the manager of the personnel department to discipline the salesmen who are under his control. As has been said, the salesman is temperamental; "the fundamental problems of sales organization are not mechanical, but mental; not physical, but psychological." It is necessary, therefore, to give a looser rein to salesmen than to tool-makers or mechanics or the clerical force. Nevertheless, the sales organization must be loyal to the house and to its policies. All salesmen must be held in check, so that their efforts can be directed by the manager. Undoubtedly, the best control of a sales organization is secured by developing good will on the part of all salesmen through fair treatment on the part of the management. When a salesman, however, becomes obstructive or has shown his incapacity, the manager must dismiss him.

**239. Advertising Department.**—Of equal importance with the personnel department is that of the advertising manager; his duty is to prepare the advertising campaigns which the company decides upon. He must have charge of the bulletins and he must be responsible for the house organs which are published. All publicity campaigns are under his direct control. More will be said of the advertising manager and his particular duties in a later section of this chapter.

**240. Sales-Promotion Department.**—The active policy of a mercantile establishment will manifest itself in a department whose duty it is to extend the business of the company. This function may be undertaken by a special department which has been called the sales-promotion department. The specific functions of such a department are to analyze the market for the purpose of directing sales, to afford the testing of new ideas, the securing of information, the analyzing and presenting of information to the sales manager. The function of sales promotion, however, may be the joint effort of various employees under the sales manager.

**241. Keeping Records.**—It is necessary for intelligent effort that records of achievement should be kept in such manner as to render them immediately available. The keeping of records, therefore, is a distinct function in itself. If the volume of business done by the company is great enough to justify it, this task may be given to a separate department. If this is done, the specific activities of such a department would be the determination of sales quotas, the inspection of orders, the checking up of expense, the adjustment of salaries, the giving of commissions and bonuses. The solution of all problems of remuneration can logically come only from the true records of activities. Many sales managers have found it a wise policy to keep the records of the salesmen in some public fashion, such as a chart or graph on the wall, in order to stimulate rivalry among the force. In such a case, every man is judged on the basis of his own achievement. The material for the construction of such charts would come from the records department.

**242. Coordinating the Force.**—The real task of the sales manager is to organize the sales force in such a way that all the parts are working together. One of the most difficult problems in coördination is the relation of the sales manager to the advertising manager. The usual practice is for the sales manager to be the superior officer. Sometimes, however, the two are of equal importance in the organization, each working independently of the other and both responsible for their actions to the general manager. In such a case, it is the duty of the general manager to coordinate the sales force. It has been found frequently that the sales manager and the advertising manager work at cross purposes. There has been jealousy of authority, of power, and of results. As a matter of fact, the advertising manager has had to fight his way to recognition.

Advertising, however, is one form of salesmanship. The advertising manager is a salesman. In some way or other, by means of organization, all advertising effort must be coördinated with the sales effort through salesmen. Behind advertising also must be the house policy and the general sales policy. The character of the commodity will likewise be a large factor in determining the character of advertising. The market, too, is an essential consideration. The problem of the commodity in its relation to the market is a common problem for the entire sales department and is in no way confined to advertising.

It may be said, in general, that advertising sells to people in large groups, while the salesman deals individually. The difference in method has been compared to the use of a rifle as contrasted with that of a shotgun. The salesman aims at individuals, the advertiser at the mass. As has been said, "The salesman appeals to the man, the advertiser to men."

The primary duty of the sales manager, therefore, is to coördinate all sales forces and to concentrate them upon a definite plan. This manager must prepare the plans and must administer them. The inside sales force, the traveling salesmen, and the advertising manager must all work harmoniously toward a common end. Otherwise, there can be no effective sales organization.

**243. Advertising Manager.**—Advertising has recently become a recognized profession. The work of the advertiser is only just now defining itself. In general outline, it can be defined as follows.

In the first place, the advertising manager must adjust the goods to the market which he is to reach. The first requirement is that he shall know how to sell. By carrying his practical salesman's knowledge into advertising, he can make his campaigns far more effective.

The general requirement of the advertising manager is that he shall have business imagination. This means that he must have a vision of the program which he is to carry out in its relation to the public. Behind this vision, however, there must be an adequate knowledge of the facts of business. The advertising man, like the salesman, should be versed in the internal problems of the business, in the competition which the business must meet, in the attitude of the dealers who handle the goods. Like the sales manager, also, the advertising manager must be a successful administrator. That is, he must see that the policy which he adopts is actually carried through.

It is a part of the task of the advertising manager to outline the general sales campaign. He needs help often from the sales manager, but he must have final authority in the selection of media and in the construction of "copy." "Ninety-nine out of 100 good advertisements are an evolution and not an inspiration." It is necessary that the advertising manager have initiative. Imagination will be of little service unless the advertising manager has sufficient aggression to make it materialize. Generally speaking, the advertising man is the experimenter in the business organization. His mind is constantly seeking new methods of reaching the market. He is searching daily for new appeals. If he is of the right type, he will abstract himself from the business and study the whole problem from an impersonal point of view. It is ability to do this which has given independence of thinking to the advertising manager.

Like the other salesmen, he needs a special course of training. He should, of course, first study the product or line of goods which he is to sell. He should be able to evolve, to originate, and to formulate effective selling arguments. He must also have a thorough knowledge of the value of newspapers, magazines, and other means of reaching the public. "The publisher can guarantee that his paper has a certain circulation, but he cannot guarantee that your advertisements will be read." It is a part of the task of the advertising man to be an expert judge of the value of space. As a matter of practice, many advertising managers have developed from the sales force. These have been the men with those peculiar characteristics which advertising demands. A great many advertising managers have come over from newspaper work. "As a matter of fact, no business experience is without value to one in the advertising business. The closer he has come to selling conditions, the better advertising man he makes. It is a mistake to assume that writing ability and a knowledge of type are an advertising man's requirements."

**244. Advertising Agency.**—In case the business is not large enough to justify an advertising department of its own, these functions may be performed by an outside agency. There are in the country a great many advertising agencies which act as advertising managers for business firms. The origin of these agencies was that of space brokers. The original advertising men bought and sold space in magazines and newspapers.

It is for this reason that emphasis has been laid upon the ability of the advertising man to know the value of various newspapers and magazines as a medium for advertising. It is necessary for the agency also to furnish expert knowledge of such things as population, circulation, climate, and superiority of morning newspapers over evening newspapers, or *vice versa.*

From the function of the old-time agency which was to solicit accounts, new agencies have developed which are headed by real business experts. They are in fact professional men. It is also important to observe that these agencies become more and more proficient as they accumulate facts and experience. Like wine, the agency should grow better with age. It is possible to-day for any merchant or manufacturer to secure professional advice on commercial problems from these agencies. For this service, a commission of from 15 to 20 per cent on the amount of advertising is usually paid.

The ideal advertising agent has been described as follows: "The good advertising agent is a high-grade business adviser. He offers the customers ideas and practical aid born of experience, together with a real concern as to the customers' success. Advertising is to-day but one feature of the work of a real agency."[1]

Some magazines have developed advertising departments which offer the same services as the independent agencies. A few of these departments offer to prospective advertisers the full benefit of their expert knowledge. It is the claim of one such department that it knows more about the business of many manufacturers throughout the country than they know themselves. The object of such study and analysis is, of course, to demonstrate the value of advertising through their columns.

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[1] *Selling Forces,* pp. 68-70.

**245. Research Department.**—Another recent development in sales organization is the research department. This is, in fact, the laboratory of the establishment. Facts are secured from various sources and are analyzed by experts who present the results of their analyses to the sales manager. It has been found in many cases that the research department is an effective means for securing coöperation among all the departments under the control of the sales manager. A more fundamental knowledge of commercial problems is demanded to-day of all progressive merchants. There is no doubt that the research department will have a much greater development in the future.

**246. Sales Conferences.**—An excellent means of educating, coördinating, and getting effective team-work from the sales force is the conference. This usually is under the direction of the sales manager and may be called on special occasions or at specified times. The frequent practice is to devote Saturday mornings to such a conference. The experiences of the past week are brought before the members of the conference for discussion and for general enlightenment.

Also, the problems of each salesman can be brought up for discussion and solution. The best business brains of the establishment can thus be brought to bear on the difficult problems which face salesmen from time to time. It is especially important that traveling salesmen should meet with the sales manager and other co-workers for an open discussion of the work that they have done and have to do.

It is possible, therefore, for the sales manager to use a conference as a means of instructing his salesmen. Into the meeting will come the best men from the force and all will get the advantage of the expert knowledge and experience of these leading salesmen. A new policy can be quickly put into operation by means of the conference. A wrong tendency can also be corrected by the same means. All such conferences should be held on the company's time.

It is possible for the inside force to benefit from conferences. Sometimes, there is special instruction for the entire sales force within the establishment. Generally, on such occasions, some one gives a talk about the merchandise of the special department, or of the store as a whole. Experience has shown that these conferences have not only value for salesmanship training, but also a very decided value for improving the morale of the selling force. Such general conferences can be addressed either by special men, or by experts from the outside.

**247. General Considerations of Salesmanship.**—At the basis of all study of salesmanship should be the belief that selling is essentially service. It follows, therefore, that the task should be done worthily. If selling is to reach the plane of dignity which it deserves, there is the obvious need for a higher degree of education and training. In many respects, the task of selling needs to be given dignity. One of the first steps in this direction is to secure a fair reward for the sales effort.

A difficult task in making salesmanship better is to eradicate all the so-called tricks of the trade. There are many devices known to salesmen for tricking the customer into buying more than he wants, what he does not want, or one article when he has asked for another. As has been pointed out, the customer has become less and less able to judge goods for himself. He pays the price asked, and learns of the quality only when he has used the commodity. Obviously, the true standard of salesmanship is to have honest goods honestly sold.

A further consideration of the selling problem is that some measure should be taken to eliminate the possibility of the salesman making errors, either in measuring or weighing a commodity sold. It is clear that if quantities are weighed incorrectly, there will be a constantly accumulating error in the transaction. If more cloth is sold than is paid for, even by a few inches, the total loss assumes substantial proportions. Various clever machines have been invented for preventing errors of this sort. It is not a matter of dishonesty, but of human nature.

A problem for practical consideration is to secure an adequate sales force to take care of the peak of the load during the day. It may be necessary to secure added salesmen for the Saturday trade or for special holiday occasions. There is the usual surplus of salesmen to call in for such continually recurring periods. A more difficult problem however arises from day to day. During the morning hours, there is a difference in the number of people entering the store for the purpose of making purchases. The very early morning hours will be lax times. The middle of the morning will show an increase in the number of purchasers, with the peak coming between eleven and twelve o'clock. There is then a decided falling-off in number until the middle of the afternoon. Another spurt of selling will come just before the closing hour. How a merchant can take care of these rush moments and at the same time not burden himself with a force that will be largely idle at other times is a very difficult question. Some merchants have met this problem by keeping the sales force busy in preparing for the rush periods. This has been done by putting commodities in packages or arranging them in such amounts as are usually purchased. In this way, a smaller number of salesmen can take care of the rush periods.

A salesman is an educator in wants. A part of his task is to create new desires among the customers. It should be his aim on all occasions to work for an increase in those wants that will contribute to general human welfare. To urge upon the customer what is detrimental to his health or what will fix upon him an unfortunate habit is unethical in salesmanship.

Selling is no longer a matter of "putting something over on the customer." No business is permanently founded that has not established good will among the large group of its customers. There can be no deception for a long period of time, because the customers will discover the inferior qualities of the goods by use. Besides, if a merchant establishes a policy that the customer is always right, it is the duty of the salesman to see that he is not in any way deceiving the customer as to quality or quantity or price.

Selling should be made an interesting and stimulating occupation. As many writers have shown, the best method of securing interest is to give the salesmen a full knowledge of the commodities which they sell. The commodities then become more than mere articles, since they take on personality and individuality. If the salesman also is interested in people, there are constantly new individuals to be observed and studied, and there are countless interesting observations to make. It is undoubtedly out of an interest in merchandise and an interest in people that the salesman will find his stimulation.

There are two kinds of salesmen. One is the general salesman who sells many kinds of commodities, and the other is the special salesman who concentrates on a certain line of goods. The capacity and the training of these two types of salesmen will naturally be different. The special salesman will probably be an expert. He will need peculiar training in order to secure the expert knowledge. The general salesman will correspond to the practitioner in medicine who takes all kinds of cases that come to him. The special salesman will correspond to the specialist in medicine who has concentrated his efforts on mastering a certain branch of the general field. Undoubtedly the special salesman will find a greater reward and greater interest and a greater stimulation in his work.

The salesman is a personal representative of the mercantile establishment. His actions and his personality will represent to a large number of people the policy and the personality of the house. There is, therefore, a responsibility on every salesman to represent worthily the merchant who has secured his services. In this way he will become a part of the sales organization that works harmoniously for their common success.

## SUGGESTIONS FOR STUDY

The student should study the sales organization in some individual establishment which handles the commodity that he is investigating. The following subjects will serve for classroom study:

### *Selecting the Sales Force*

1. The legal problem.
2. The human element in business relationship.
3. Standardizing the salesman.
4. Analyzing the selling forces.
5. The psychological factors.

### *Training the Sales Force*

1. Vocational education.
2. Professional education.
3. School system of education.
4. Training and experience.
5. Organized training by individual businesses.
6. Theoretical training *vs.* practical experience.

### *Organizing the Sales Force*

1. Lines of authority in sales force.
2. Functional relationships.

3. The consumer and sales organization.
4. Individuality in a sales organization.
5. The external and the internal problem of organizing salesmen.
6. Temperament in sales organization.
7. Specialization in sales organization.

READINGS:

*Library of Business Practice:* vol. iv, Part II, Chap. IX, "Hiring and Handling Salesmen"; vol. iii, Part III, Chap. XIII, "Where to Find the Best Salesmen," Chap. XVIII, "Building Up a Retail Sales Force"; Chap. XVI, and XVII; vol, iv, Part II, "Organizing and Managing the Sales Force"; Chap. X, "Team Work Among Salesmen"; Part III, Chap. XIX, "Using Coöperation to Build Salespeople."

Brisco, *Fundamentals of Salesmanship,* Chap. XXII, "Hiring"; Chap. XXIV, "Training"; Chap. XIX, "The Manager and the Sales Force."

Maxwell, *Salesmanship,* Chap. VIII, "Management of Traveling Salesmen."

Weld, *Practical Salesmanship,* pp. 92-160.

Jones, *Salesmanship and Sales Management,* Chap. IV.

Shively, *Salesmanship,* vol. ii, Chap. III.

*Printer's Ink,* May 11, 1916, p. 85; April 20, 1916, p. 38; August 5, 1915, p. 33; February 4, 1915, p. 104; February 24, 1916, p. 37; January 27, 1916, p. 10; November 7, 1915, p. 102.

Farrington, *Store Management Complete,* Chap. VI, "Clerk Management."

Sheldon, *The Art of Selling,* pp. 11-36.

Hirschler, *The Art of Selling* (Retail), Part I.

Hall, *Short Talks on Retail Selling,* pp. 8-19.

Hoover, *Practical Salesmanship,* pp. 99-165.

Leigh, *The Human Side of Retail Selling.*

Moody, *Men Who Sell Things,* Chap. XII, "Right Kind of Salesmen."

Alexander Hamilton Institute, *Marketing Methods and Sales-*

*manship,* Part III, Chap. II, "Selecting Men"; Chap. III, "Training Salesmen."

Nystrom, *Retail Selling,* Chap II.

——, *Economics of Retailing,* Chap. VI.

Blackford, *The Job, the Man, and the Boss,* Chaps. VI, VII, VIII, IX.

Madden, *Selling Things,* Chap. II, "Training the Salesmen."

*Modern Business,* vol. iii, Chap IX, "Methods of Training Salesmen."

Fisk, *Retail Selling,* Chap. IV, "Organization of Sales Force"; Chap. XI, "Retail Selling, Training for Retail Salesmanship."

Hoyt, *Scientific Sales Management,* Chap. I, "Two Kinds of Salesmen"; Chap. III, "What Is Scientific Sales Management?"; Chap. X, "Councils, Meetings, and Conventions"; Chap. XVI, "Hiring Salesmen."

Frederick, *Modern Salesmanagement.*

# CHAPTER XX

## ECONOMICS OF ADVERTISING

**248. The Study of Advertising Media.**—The business dictum has gone abroad that the merchant must advertise to live, and that the advertising must be continuous and comprehensive. Whether this dictum is rooted in experience or whether it is nourished and tended by those who have advertising space for sale may still be an open question. But that the grand total sum of money spent for advertising in this country is stupendous is not to be doubted. It has been estimated that it reaches a billion dollars annually. Experts have arisen to act as guides in this vast expenditure. All sorts of media have been devised and used. This new business force has entered as a disturbing element into business relations.

Advertising has seized upon newspapers and magazines whose primary purpose was literary, and by extending its financial power has threatened to dominate the policies of those media. The financial powers behind the advertising columns have been accused of coloring news, and of controlling the political, economic, and social policies advocated. This situation has created some big social problems.

Many businesses have developed their own media of advertising in the form of house organs. This is a highly specialized medium and is probably limited in its influence and possible development. Others have sought to utilize their manufacturing and mercantile establishments as aids in advertising. Hence, unusually attractive buildings are erected, and windows are carefully trimmed to afford the greatest lure for prospective purchasers.

The media used in spending the billion dollars every year are too numerous to count. Advertisements shout at us from field and wood; streets are lined with them, the landscape is dotted with them. There are all sizes and shapes and colors; light, color, electricity, and mechanical ingenuity are being pressed into the service of advertising. And the end is not yet.

What one or what combination of these multitudinous media is best for a given commodity? That is a big problem of sales management. Economists say that the success of advertising depends directly upon the amount of money available for this use; the business with practically unlimited funds will succeed. There are, of course, modifying factors. The size of the market to be reached and the character of the market are two of these factors to be considered. There must be many more, such as the nature of returns desired, business habits, cost, relation to existing distributive organization, and others.

No advertising medium can be adjudged justly until some adequate measurement of returns may be had. This measurement is in itself an exceedingly difficult matter, but it underlies the whole process of determining whether or not advertising really pays, directly or indirectly, immediately or in the long run.

**249. What Is Advertising?**—Advertising is so varied in character and shades off so imperceptibly into other methods that no dogmatic, definite explanation of its scope will suffice. It has been called "salesmanship on paper," performing the same function as any member of the sales force. There is, too, a "preparing the way" theory of advertising, which points out the fact that advertisements are suggestive, educational, but they do not close a sale.

The Supreme Court of the United States has essayed a definition as follows: "Advertising is mere identification and description, apprising of quality and place. It has no other object than to draw attention to the article to be sold."[1]

A criticism of this narrow definition of advertising has been made:

> There is no place for the educational advertising campaign, the development of new wants; there is no place for an advertisement whose purpose it is to sell a certain make of goods where there are a half dozen of equal quality at the same place. . . . Has the learned judge never delved into the new business of advertising? Does he not know of the eager study of methods of appeal, of the principles of psychology, of art, of color effects, of design, of the power of words? Has he never seen any appeal to cupidity, any "insidious potentialities," any "lure to improvidence," any seductive power on wall and tree, in street car, and on magazine and newspaper page? Is there no "insidious seduction," no lure in legalized "puffing" of one's goods?[2]

It may thus be seen that advertising has greatly broadened in recent years. Undoubtedly, there is an almost infinite number of devices to which tradesmen, wholesale dealers, and manufacturers resort to promote the sale of their goods. All of them are advertising. And so is the "puffing" of a candidate for office, the appeal for funds, and almost any form of propaganda. Advertising in trade is any method, other than through personal agents such as salesmen, for increasing the sales of one's goods. When there are similar methods used outside of trade, they may also be called advertising in a very broad sense.

On this basis, advertising is of two general kinds; one is direct and the other indirect. Announcing the character of one's goods through the columns of a newspaper or a magazine, by bill boards, by street-car cards and electric signs, is an indirect method. The use of a sales letter is a direct method.

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[1] Rast *v.* Van Deman, 240 U. S. 360.

[2] Duncan, *Journal of Political Economy,* vol xxiv, p. 947.

In a very vital sense, advertising serves as a dynamic organizing force in merchandising manufactured goods, just as trade information serves as a dynamic force in dealing with raw materials and foodstuffs. The subject matter of advertising is trade information. It results from an analysis of a commodity in relation to human wants, actual and potential.

**250. Character of the Commodity and Advertising.**—In studying advertising as an economic force, a practical query is whether or not every commodity is susceptible to being advertised. The great bulk of raw materials and foodstuffs passing through the market are not advertised. Many manufactured goods, also, are handled in the market without advertising. Is it possible to apply this force to all kinds of commodities?

As has been shown, advertising is a species of selling. It is, in fact, selling goods, largely at long range, by description and by sample. Clearly, therefore, an individual commodity may be described and sold by this method. A sample, however, requires that all individual articles must have the same characteristics as the sample. In other words, selling by samples requires standardization. Generally speaking, effective advertising can be applied only to those commodities that are standardized.

Standardization of commodities, however, may apply either to physical characteristics or to quality. A certain manufacturer or jobber or retailer may have established for himself a quality reputation. Consumers, through experience, have grown to accept the goods which these business men handle as of certain grade or quality. On the basis of this kind of standardization, even style goods, which are so classed because each, individually, has distinct characteristics, may be advertised. It is possible, also, on this same basis to advertise goods that are made on order.

Generally, standard goods are also goods that are trademarked, or given trade names for the purpose of identification. The most effective advertising is, therefore, to be found in the cases of goods that have been identified. There is probably a relationship of cause and effect that works reciprocally at this point. That is, the tendency to standardize goods results in identification of those goods. On the other hand, the endeavor to identify goods leads almost inevitably to some form of standardization.

It is interesting to note in this connection that the methods of merchandising manufactured goods have been applied with success to the marketing of citrus fruit, raisins, lumber, and other foodstuffs and raw materials. In these cases, however, there has been careful attention given to grading, which is an obvious attempt to standardize these goods. It is clear, therefore, that the group of advertisable goods is being rapidly enlarged.

It is important to consider further, in respect to advertising as applied to various kinds of commodities, whether or not these goods are old, established goods or new lines. The kind of appeal and the methods used will vary in these different cases. Under the business dictum that a merchant or manufacturer must advertise or perish, it is clear that even those goods which have an established reputation in the market must still be advertised in order that they may hold their place. On the other hand, the selling of new goods and new applications to human wants of established goods can be secured by educational advertising. The preliminary step in the solution of the advertising problem is a thorough analysis of the commodity.

**251. Character of Market and Advertising.**—It is likewise necessary to analyze market demand before determining upon an advertising plan. The interests and business habits of the prospective consumers, their illiteracy, their prejudices, a knowledge of what they read, of where they go, are all parts of the problem. No appeal can be effective unless it is adjusted to all these characteristics of the group of people to whom the appeal is made. To advertise without comprehensive and thorough market analysis is as uncertain in results as the proverbial casting of bread upon the waters.

The two cardinal principles of advertising are that it must be persistent, and it must be intelligent. The goods are to be kept always before the eye and in the mind. Especially is it necessary to suggest the goods at those times when they may be particularly desired. In rural churches where palm-leaf fans are distributed by the enterprising advertiser, the advertisements on them will largely apply to those commodities which are most to be desired by people in hot or stuffy rooms. Cooling drinks are emblazoned on all the fences at baseball grounds. Advertising managers have been energetic and aggressive in following out this general principle.

Many advertisers, however, have made the grave mistake of applying too generally the principle which they have found effective in certain regions. For example, American manufacturers have attempted to establish a market for their commodities in South American countries where the illiteracy of the people approaches 95 per cent by using the same methods which they have used in the United States. But the most illiterate people can be impressed by pictures, and by appeals to the ear and eye. It is for this reason that a manufacturer of sewing-machines has successfully identified his product in various foreign markets by a distinct sign. Those who see this sign are not supposed to read what is there printed, but to associate it with the article itself. Many trade-marks in the

Chinese market are not understood by the buyers, but they nevertheless stand for certain qualities, and thus prove effective sales media.

Advertising should also be made to suit the taste of the prospective consumer. Some people are not only not attracted by flaring colors and crude pictures, but are even repelled by them. There are many people, too, who feel that certain attractive bits of natural scenery or certain places of historic interest should not be used by any merchant to advertise his goods. In other words, the *finesse* of personal salesmanship should be used in developing methods of advertising. The advertising manager has as great a need of studying the consumer as has the sales manager.

**252. Size of Market and Advertising.**—Just as the market area for any given commodity may be either local, national, or international, so likewise the advertising campaign to sell these commodities may be local, national, or international. The manufacturer of products for general consumption is particularly interested in national or international markets. The jobber, also, desires to extend the boundaries of the market for the commodities which he handles and develops a national or international advertising campaign. In general, the retailer is a local advertiser for the simple reason that his market is a local one.

It is obvious therefore that the character of advertising will be modified to a considerable extent by the size of the market. The medium which is selected will be determined finally by this factor. A magazine of national circulation will not be used by the local dealer. The national advertiser cannot consider as carefully the local conditions of any market center. Large-scale production in the United States has tended to develop rapidly national advertising campaigns.

**253. Selection of Media.**—Apart from the subject matter of an advertisement, there is the selection of the medium which is to carry it. The previous discussion has developed the fact that the "copy" of an advertisement will result only from the study of the commodity and the market for it. In so far as advertising is a sales method, it is necessary to study the selling points of a product, that is, the utilities of the given commodity. The results of such study can direct the selection of the market by class, by geographical location, by business habits, etc. There is a great variety of media which the advertiser may use. A number of the chief ones will be discussed in this section. They may be divided into the following classes: newspapers, magazines, house organs, business letters, outside advertising, street-car advertising, and window-displays. Some consideration also is given to the means peculiar to mail-order houses that sell through the catalog.

**254. Newspapers.**—The newspaper is to be distinguished from the magazine chiefly on the basis of the time of its appearance. It is published more frequently than any other kind of periodical which its readers receive, and it carries as its mainstay a great volume of local and ephemeral news or gossip. Classified on the basis of the time of its appearance and the character of material which it carries, the newspaper may be termed a daily, weekly, semi-weekly, or Sunday publication. There were in the United States in 1916 some 2,500 newspapers of which practically 600 had Sunday editions. There were about 14,000 weekly and semi-weekly newspapers in the United States. In thirty-two of the fifty cities in the country with a population of 100,000 or over, there were 119 daily newspapers with an average circulation in excess of 50,000. The total circulation of these 119 dailies was 15,649,634. The total circulation in 1914 for the daily newspapers in the United States was about 30,000,000 copies. More than 1,000 of these daily newspapers have weekly or semi-weekly editions. The Sunday newspapers of the United States have about 17,000,000 circulation and the weeklies and semi-weeklies about 24,000,000.

An estimate was made in 1911 as to the amount of advertising carried by the newspapers of the country. This estimate put the amount of money invested in retail and general advertising in the columns of the newspaper at $250,000,000.[3] Undoubtedly, with increased circulation and increased cost of publishing, the amount to-day is considerably beyond this.

It has been said that these daily, Sunday, and weekly newspapers furnish the cheapest and most serviceable means of disseminating information, general and local, to the 105,000,000 people in this country. Practically every community and every town of any size in the United States has at least one publication of this kind devoted especially to local affairs. It becomes necessary, therefore, to study carefully this medium for carrying advertising matter.

The analysis necessary for intelligent use of newspapers as advertising media will include the following points: (1) the reputation of the paper; (2) the general make-up and tone of the paper; (3) the class or quality of subscribers; (4) the character of the paper, namely, whether religious, political, financial, etc.; (5) essential facts of circulation; (6) the number of editions and the time of issue; (7) the kind of advertisements which it carries. It is also to be considered that the newspaper is a tremendous concentrating force, more rapid, more thorough, and more effective than almost any other means of local stimulation.

The case for using newspapers as a medium of advertising may be stated under the following heads: (1) it reaches all classes of readers intensively; (2) it promotes local emphasis; (3) if attention is gained, the advertisement will reach a larger percentage of a given group in a given time than any other medium; (4) it is the medium to use for quick returns; (5) it can take advantage of local incidents. It has been said that "as an advertising medium, the newspaper displays its greatest strength with commodities which are of general interest to the people, and in more or less general use."

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[3] *Printer's Ink,* May 4, 1911, p. 78.

Against the use of newspaper columns for advertising, it has been said that there is a general lack of definite business policy behind them. There is also an absence of any concerted attempt to supervise the character of advertisements that are accepted. It is further held that "while there are many important exceptions, the newspaper is the last stand of the stock swindler, the real estate swindler, the patent medicine and cure-all fake, and the rest of the brotherhood who have so long taken advantage of the force of advertising to separate the gullible portion of the public from its money without returning value in proportion."[4]

**255. Magazines.**—There are various types of magazines and other periodicals which may be classed with them in the United States. The figures for January 1, 1917, are as follows:

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| Class and trade publications | 4,200 |
| Religious publications | 850 |
| Farm journals | 500 |
| Secret society publications | 250 |
| Publications of general circulation: | |
| Magazines | 117 |
| Women's publications | 39 |
| Mail-order publications | 29 |
| Total | 5,985 |

This list obviously does not include the 3,000 or more trade papers that are issued by trade associations in this country. Of the publications of general circulation, 106 have a combined circulation of more than 23,500,000. The 39 women's publications have a circulation around 24,500,000. The circulation of the 29 mail-order publications is estimated at about 16,000,000. Thirty-eight of the 850 religious papers have a circulation of more than 100,000 each. There are 49 farm journals with a circulation of more than 100,000. There are, of course, the popular weekly magazines that have passed far beyond the million mark in circulation.[5] These, too, are clearly a force to be reckoned with as advertising media.

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[4] *Cf.* Tipper, Hollingworth, etc., *Principles and Practices of Advertising.*

Magazines may be classified on the basis of the interval between issues into weekly, bi-monthly, monthly, and quarterly magazines. On the basis of the class of people to whom they appeal, magazines may be classed as general, trade journals, women's publications, etc. Each of these classes will be suited to particular kinds of advertising.

The arguments for the use of magazines as media of advertisements are numerous: (1) the magazine reaches particular groups of people in all sections of the country, and has therefore the merit of even distribution; (2) people read magazines more leisurely than newspapers and as a result more attention is likely to be paid to the advertisement; (3) the magazine goes into the home and is placed on the library table where it remains to be read from time to time over a long period; (4) a single copy of the magazine is frequently read by several persons; (5) the magazine offers better facilities for high-grade illustrations and for the use of colors; (6) a yearly subscription guarantees the effectiveness of repetition in advertising the product.

In analyzing the magazine for its advertising possibilities, there are several important questions to be asked. It is essential to know the total amount of advertising which the particular magazine carries. One should inquire also into the recognized standing of the magazine. There are such questions as price, size, shape, color of paper, and the editorial policy of the magazine. Is it distributed by subscription or through news-stands? Is the circulation of the paper obtained by club methods, by free distribution, or by straight subscription? It is, of course, necessary to know the total circulation of the magazine, as well as its regional circulation.

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[5] Senate Document No. 79, "Book Paper Industry," p. 21, 65th Congress, 1st Session.

From the point of view of those who will likely read the magazine, one should ask about the purchasing power of the readers, their occupations, financial standing, culture, etc. The analysis of circulation should be made to include facts relating to states, to buying centers, to groups of cities, and to occupations. There is also the technical information as to the kind of plates that may be used, the closing dates, the rate cards, the various rules and regulations covering advertising matter.

**256. House Organs.**—The house organ is essentially a highly specialized medium. It is primarily intended to promote good will among the employees in a given establishment. Sometimes, however, house organs are of broader appeal and carry information that is of more general interest. There are certain house organs which take advertising matter from outside the plant. Others have a policy of excluding anything beyond the immediate interest of the establishment. As an advertising medium, therefore, the house organ is strictly limited in possibilities. It is clear that the columns of this medium cannot be open to any competitor, or any one selling goods that would interfere with the market of the firm. Coöperation, however, with allied industries is possible. The manufacturer of automobile accessories could readily admit into the columns of his house organ advertisements of those automobiles for which his products are fitted. The same is true in all allied industries. As an advertising medium, nevertheless, the house organ is of very minor importance.

**257. Business Letters.**—Most sales letters can be classed as direct advertising media. They prepare the way largely for the visit of the salesman and have to do with closing the sales contract. The letter which is sent out by many establishments carries the same kind of material as the advertising matter in other media.

The business letter can be made an effective means of bringing goods before the mind of the prospective customer. Its relation to general advertising has been likened to the general estimate as compared with a precise figure. The general advertisement is spread broadcast with no definite person in mind. The sales letter is sent direct to an individual. The success of the sales letter may, therefore, be more easily determined and its preparation can be guided by a more specific consideration.

The main characteristics of a successful business letter may be stated as follows: (1) the business letter must be, as a prime requisite, interesting to the reader; (2) the business letter should be brief and to the point; (3) the business letter should be courteous and respectful and simple and direct; (4) it should be tested by its effect upon one's self; (5) it is necessary for the writer of a successful sales letter to understand clearly the situation which is to be stated by the letter; (6) the good sales letter is characterized by absolute sincerity; (7) the form of the letter, the paper, the heading, the type, and all the physical characteristics must be pleasing and effective. In general, the sales letter should be given the same careful consideration that is given to any other phase of the sales campaign. No carelessness, either in expression or in the making of the letter, should be permitted. Good sales letters are a work of art.

**258. Outdoor Advertising.**—There has been a rapid development of facilities for outdoor advertising. These will include electric signs, billboards, and every other device for bringing the commodity to the attention of the passers-by.

The arguments for using outside media for advertising are chiefly as follows: (1) outdoor advertising is valuable because of its flexibility. It permits concentration at any geographical point, and it may be confined to a state, to a city, or to a single block; (2) outdoor advertising claims that there is no waste in its circulation. As a matter of fact, it does not circulate—it stands in the way of the passing throng; (3) the advertisement on the billboard or sign is "alive" all the time; (4) there can be carefully planned coöperation between the selling force and the simultaneous appearance of posters; (5) there are many realistic possibilities in posters, as human figures, or interesting scenes, or attractive reproductions of the commodity itself may be used; (6) there are also many possibilities in the effective use of colors; (7) the advertisement placed in outdoor advertising is carefully censored by billboard companies; (8) this means of advertising is applicable to both local and national advertising; (9) outdoor advertising can be used to reënforce other forms of advertising; (10) it can be so placed that its message is concentrated at one strategic point.

**259. Street-Car Advertising.**—With the development of street railways, there has been at the same time a constantly growing use of street-car cards for carrying advertising matter. It is argued that the space above the windows of the cars would otherwise be wasted, and that the passengers are able to divert themselves by reading what is written on these cards.

Street-car advertising has really no circulation. What corresponds to the circulation of a newspaper or magazine is the number of people who read the cards in the cars. It has been estimated that the number of passengers daily for each car in the United States averages between 600 and 800, exclusive of free transfers. The number of cars in the United States is approximately 50,000. The total number of passengers daily, therefore, ranges between 30,000,000 and 40,000,000. Annually, the number would be between ten billion and twelve billion. It is also declared that the number of daily passengers on street cars will closely approximate the population where these cars are run. In Philadelphia, where the population is 1,800,000, the average number of passengers daily has been estimated at 1,600,000. In Chicago, the annual daily average for eight years on the elevated roads alone was 1,200,000. Futhermore, it is argued that more than one-half of the population of the United States lives in the cities, and therefore street-car advertising covers more than one-half the total population. This calculation, however, does not take into account the fact that the same people often ride several times in one day.

The case for street-car advertising will include these points: (1) the street-car card reaches a great number of people intensively in a given area; (2) street-car advertising can be used to advantage, either by national or by strictly local advertisers; (3) the passenger can read the cards at leisure, is in a receptive mood, and the impression is easily and definitely made; (4) the so-called "time exposure" of the street-car card, that is, the period of time during which the passenger faces the card, is on an average between fifteen and thirty minutes; (5) there is a strong element of repetition in street-car advertising, cards are seen by the same people each day, sometimes twice, sometimes three or four times, for the majority of passengers repeat their rides; (6) the street-car card has also color possibilities; (7) street-car advertising has an element of flexibility, it may be confined to a single car line, or it may cover the entire city. It is said that in New York City one can buy Fifth Avenue space, Broadway space, and subway space. (8) The street-car card is also protected from the weather and retains its freshness; (9) the advertising matter on street-car cards is censored by the state public-service commission; (10) the cost of this medium of advertising is relatively small, the average has until recently been about fifty cents a month. The range is from thirty cents to two dollars for the period of a month. The highest-priced surface-car rates are on the Broadway line in New York City. (11) Before the advent of the automobile, at any rate, the street-car card was a cosmopolitan medium because all classes of people rode in the cars; (12) all space is carefully standardized; (13) the cards may be purchased for a year or for shorter periods.

Against the use of street-car advertising, there have been the arguments that there is a dominant element of monotony in the cards, that all are the same size, that the position is above the level of the eyes of the passenger, and that he usually prefers to look out of the window. The cars may stand in the barns for long periods of time. These cards are relatively small as compared with outdoor advertisements. Finally, the dimensions of the card limit the advertising possibilities because of their narrowness.

**260. Window Displays.**—Merchants have for a long time realized the value of making the goods sell themselves. They have, therefore, placed merchandise within the sight of the prospective customer, either on the shelves or counters, or in the windows. Only within recent years, however, has serious attention been given to the art of window display. So far has this method of advertising been developed that it has affected the construction of retail stores and of many manufacturing establishments. A special business of window dressing has also developed and the principles of artistic effect have been studied with a view to making the retail store windows as attractive as possible.

The progressive merchant of to-day, therefore, lives in a glass house. He no longer closes his windows with shutters at night, nor does he make them narrow, so that they may be easily defended against possible burglars. On the contrary, he has given careful study to the question of securing the best possible light and the greatest possible space for the display of his goods. Certain department stores charge against the window space on the first and second floors a specific percentage of overhead cost as advertising expenditure. Experiment has shown that window displays are an effective method of advertising goods.

**261. Catalogues.**—The mail-order houses have demonstrated the effectiveness of advertising by means of catalogues. So essential a characteristic of the mail-order houses is this sales medium that they are frequently called catalogue houses. They charge against each article the amount of space which it occupies in the catalogue and maintain it in stock or drop it according to whether or not it pays its way.

Other retail establishments, as well as wholesale establishments, have proved the value of catalogues as a means of advertising. Many retail stores send out seasonal catalogues announcing special types of style goods and presenting in an attractive way the new fashions and modes of dress. These catalogues are most effective in advertising dress goods and home decorations, but may be used for many different types. In addition to the seasonal catalogue there are often special bargains that are announced by this method. Catalogues frequently are sent at the time of the visits of traveling salesmen or are sent between visits to retailers. The catalogue offers many opportunities for artistic effect and frequently proves to be an effective means of educational advertising.

**262. "Dealer Helps."**—Manufacturer, jobber, and retailer have certain interests in common. It is to their mutual advantage, for instance, to sell as great a volume of goods as possible, if the margin of profit is satisfactory. Within this field there is a splendid opportunity for coöperation. Manufacturers have found it to their advantage to assist their dealers with various kinds of advertising material. These may consist of window-displays, or calendars, or other media. Many manufacturers coöperate with the retailers in local advertising campaigns.

The jobber is also interested in coöperating with the retailer for the purpose of selling the largest possible volume of goods. He may, therefore, furnish the dealer with various kinds of window-cards or other announcements and, like the manufacturer, may share the expense of local advertising campaigns.

Whenever the manufacturer or the jobber joins with the dealer in an advertising campaign, the coöperation is usually called "dealer helps." Underlying this entire movement are the problems of identification and control of consumer demand. The manufacturer and the jobber, by advertising for the purpose of developing good will, have become identified with the goods in the minds of the consumers. The retailer, under these circumstances, runs the risk of becoming nothing more than an order taker. Within a limited area, however, coöperation in sales effort can be made mutually helpful.

**263. Demonstrators.**—In the sale of those goods which require special knowledge on the part of the consumer, or for which he requires education, demonstrators have been found an effective means of advertisement. The manufacturers of such goods will frequently place in the retail store demonstrators whose purpose is to develop new wants or to teach the consumer how to secure the best satisfaction from the goods. Jobbers may use the same method. Even the retailers may find this a successful means of selling such goods. The use of demonstrators is sufficiently important to require special attention.

**264. Checking Up Returns.**—One of the most difficult problems connected with advertising is the determining of returns. These results may be either one of two kinds: immediate, or direct, results, and long-run, or indirect, results. Many instances have been cited where the return on a definite advertisement has come after the merchant had ceased handling the goods and the manufacturer had ceased to make them. Only an estimate can therefore be made of the direct results of advertising. Indirectly all advertisements work continuously, so long as they remain in the minds of the consumers.

Various devices have been suggested, most of them of a mechanical character, to check up advertising results. Advertisements have been "keyed" by inserting a figure or letter or by some other simple device, so as to identify all correspondence with the particular kind of advertisement. All of these devices are helpful and will enable the advertiser to plan his campaign with greater intelligence. On the whole, however, the advertiser must be willing to wait for long-run, indirect results.

## SUGGESTIONS FOR STUDY

The student should study at this point the economics of advertising in connection with his special commodity. The following will serve as topics for classroom discussion:

### *General—Media of Advertising*

1. Definition of medium.
2. Medium and the product.

3. Medium and the market.
4. Medium and returns—direct and indirect.
5. Medium and business habits.
6. Cost of media, basis of charge, unit used, wastage, etc.
7. Social control of media.
8. Media and the distributive organization.

### *Magazines and Newspapers*

1. Newspapers *vs.* magazines as media.
2. Analysis of circulation data.
3. Media and news.
4. Advertising rates.
5. Media and national advertising.
6. Media and literary articles.
7. Psychological factors in these media.
8. Advertising and editorial policy.
9. Classification of newspapers and magazines as to purpose, appeal, content, class of readers, methods of reading.
10. Free publicity in newspapers and magazines.

### *House Organs, Trade Journals and Other Publications of the Sort*

1. Origin and development.
2. Compare with periodicals and newspapers as to circulation, cost, content.
3. Elimination of wastage.
4. Value of technical information.
5. Compare and contrast technical and trade journals.
6. Show where these specialized media fit into the distributive system.
7. Sum up their advantages and disadvantages.

### *Window Displays*

1. Origin and purpose.
2. Relation to the distributive organization.
3. Cost of displays.

4. Value of motion, color, and light in displays.
5. Displays and dealer service.
6. Who pays for this form of advertising?
7. The contest for the dealer's window.
8. This medium as related to the character of the commodity.
9. Window displays and dealer's profits.
10. What should go into a window display?

### *Outdoor Advertising*

1. Define "listed," "protected," "renewed," "guaranteed," postings.
2. Cost data for outdoor advertising.
3. Methods of securing outdoor space.
4. The appeal of outdoor advertising.
5. What outdoor advertising should contain.
6. Social point of view in outdoor advertising.
7. What classes of products are adapted to outdoor advertising.
8. The kind of returns expected from outdoor advertising.

### *Street-Car Advertising*

1. Cost data in street-car advertising.
2. Psychological considerations in street-car advertising.
3. Products adapted to this kind of advertising.
4. Standardization of street-car advertising.
5. Social point of view in street-car advertising.
6. Kind of returns from street-car advertising.
7. The content of street-car advertising.

### *Checking Up Returns*

1. Mechanical methods of securing data.
2. Difficulties in the way of getting reliable data.
3. Application of statistical methods to the problem.
4. The problem of immediate and remote returns.
5. The problem of frequency and repetition.
6. The problem of duplication.
7. The "laboratory method."

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# CHAPTER XXI

## MERCHANDISING COSTS AND PRICES

Somewhere between farm or shop and the consumer an increase in price of from 25 per cent to 60 per cent is made. "Forty per cent of the price paid by the ultimate consumer for a pair of shoes," it has been said, "is consumed in getting the shoes to him from the manufacturer, exclusive of the manufacturer's profit, that is, in marketing them."[1] What factors of expense have entered this price to the ultimate consumer, and what the chief determining influences are in that price are considerations worthy of particular attention. The actual figures will change from time to time, but the fundamental factors and influences will remain.

The factors of expense are the cost of the goods, including buying expense, the cost of handling them, including rent, interest, and all operating expense, and the cost of selling them, including advertising. The influences affecting price are far more subtle and intangible. Among them are demand relative to supply, competition, style, weather, climate, government control, foreign influences, custom, influences affecting allied commodities, tariff, and many psychological influences. Prices, especially retail prices, tend to crystallize into systems which enable them to withstand greater shocks, but which also make influences more widely felt when a break comes. It is proposed to discuss here some of these factors and influences in the prices of manufactured products.

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[1] *Annals of the American Academy of Political and Social Science*, May, 1915.

**265. Factors of Expense.**—The problem of determining and of allocating costs is one for the accountant. The manufacture of goods affords a wide field for cost accounting, especially as a means for more intelligent business management. Where the manufacturer, however, organizes a sales department and does advertising, he faces problems of the same kind as those of the merchant. In fact, the manufacturer becomes a merchant.

The merchant generally has been negligent in his keeping of accounts in the past. There are many organizations to-day, however, that are urging upon him the need for careful, standardized accounts. He is beginning to awaken to the fact that intelligent direction of his business demands an intimate acquaintance with costs. In aiming at an intelligent price policy, such knowledge is essential. Especially is this true for the retailer. He must know, for instance, that if he is a furniture dealer, his rent item will be the heavy one relatively. If he retails shoes, clerk hire will mount. In a retail jeweler's store, turnovers are slow and investment is heavy. In a five- and ten-cent store, the small margin of profit on each sale demands at least six turnovers of goods per year, and in a department store the rising costs of service need careful watching.

When the store is a going concern, the initial expenditure in the merchandising cycle is for the goods themselves. This is an investment problem, for the working capital is tied up in the stock until it is returned through sales. The expenditure should be made only upon the basis of a full knowledge of the goods and the market. Goods are bought to be sold at a profit, and the purchasing must be done intelligently. It has been estimated that in retail shoe stores the buying expense, that is, the percentage to be charged to the expense of the purchasing department or to the buyers, ranges from .8 per cent to 1.8 per cent of the net sales.

The cost of handling goods includes the freight, the cartage, receiving, unpacking, storing, rent, interest, and minor items such as insurance, heat, light, taxes, telephone, etc. Of these items the heaviest one is likely to be rent. Estimates for rent run from 2 per cent to over 14 per cent of sales.[2] The wide divergence is due to differences in location and the size of the town. The amount of interest will be determined by the relative expense of stock and the rapidity of turnover. For the shoe dealer, the percentage of net sales varies from 1 per cent to 7.9 per cent. The rest of the charges are variable and of minor importance. Careful account, however, should be kept of them.

Every store has its expenses for management and the office force. It is necessary to have these carefully allocated. This overhead charge must bring returns through intelligent direction and efficiently ''facilitating'' of operations.

Another part of the cost of merchandising is the cost of selling, including advertising. Of this cost there are two main items; one is the expense of the sales force, and the other is advertising in all its forms. The total expense of selling will vary with the effectiveness of management, the character of goods, the size and character of the market, conditions of business, and as to whether the establishment is a new one or one well known and long established. Certain goods at certain times may ''sell themselves''; there may be a seller's market or a buyer's market.

The variations in selling costs are shown by the following estimates:[3]

| Cost to Sell | Per Cent |
|---|---|
| Dry goods about ........................ | 23.05 |
| Groceries about ........................ | 17.91 |
| Notions in variety store about ............. | 17.76 |
| Hardware about ........................ | 20.41 |

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[2] Nystrom, *Economics of Retailing,* p. 132.

[3] *Cf.* Sammons, *Keeping Up with Rising Costs,* pp. 20-30.

| Cost to Sell | Per Cent |
|---|---|
| Clothing about | 23.47 |
| Drugs about | 24.65 |
| Furniture about | 26.51 |
| Jewelry about | 26.81 |
| Shoes about | 23.22 |

Selling by a mail-order house through catalogues, letters, and newspaper advertisements costs about 7.21 per cent of net sales. The retailers of farm machinery were paying a few years ago an average of about 17 per cent on sales. The average selling cost for manufacturers of women's muslin underwear has been estimated by Government investigators at about 7.53 per cent; the expenses for certain ones of these manufacturers ran about 3.24 per cent for sales force. The selling expenses of book-paper mills in 1916 were about $77.50 to $90 per ton. Jobbers in news-print paper claim an average cost of doing business at from 12 per cent to 17 per cent, which includes a profit.

Records from 650 retail shoe stores, upon analysis, showed the results given in the table below:[4]

| Item | Lowest percentage | Highest percentage | Percentage about which data center (not an average) | Percentage about which a concentration is sufficient to indicate a realizable standard |
|---|---|---|---|---|
| Gross profit, including discounts | 20 | 42 | Low grade 23–25<br>High grade 30–33 | |
| Total operating expense not including freight and cartage and interest | 18 | 35 | Low grade 23<br>High grade 27 | Low grade 20<br>High grade 25 |
| Buying expense | 0.8 | 1.8 | 1.1 | 1.0 |
| Salesforce | 5.0 | 10.3 | 8.0 | 7.0 |
| Advertising | 0.0 | 8.8 | 2.0 | 1.5 |
| Deliveries | 0.0 | 1.4 | 0.6 | 0.4 |
| Rent | 1.8 | 14.6 | 5.0 | 3.0 |
| Interest | 1.0 | 7.9 | 2.5 | 2.0 |
| Stock-turns | 1.0 | 3.6 | 1.8 | 2.5 |
| Annual sales of average salesperson | $5,000 | $16,500 | $10,000 | |

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[4] *Bulletin of the Bureau of Business Research,* Harvard University, No. 1, p. 14.

The paying of salesmen may be merely a simple wage, paid daily, weekly, or monthly. Or there may be, for purposes of stimulating interest and of unifying the sales effort, certain commissions or bonuses offered. Commissions, bonuses, and profit-sharing plans have proved helpful for traveling salesmen in many instances. The same methods can be used with department and sales managers.

Salesmen, on the whole, are a relatively low-paid group. The total expense for the sales force, however, is usually the chief item in selling cost and needs careful consideration. The advertising appropriation usually ranges from a fraction of 1 per cent to 5 per cent of the sales expense. The methods used in determining the amount of appropriation for advertising have been stated as follows[5] :

1. Apportioning a percentage of the gross business of the previous year.
2. Apportioning a percentage of the net profits of the previous year.
3. A progressive advertising appropriation, in proportion to the current increase over sales during the same period in the previous year, monthly or quarterly.
4. Grading the appropriation according to the plans for the ensuing year, based on constructive analysis.

**266. Commissions for Jobbers and Brokers.**—Generally speaking, the increase in price of commodities passing through the hands of jobbers or brokers is determined on the basis of a definite percentage. This percentage varies from 1½ to 3 per cent or more on the cost price. Out of this the middleman pays the expense for handling the goods and secures his profit. For the brokers, the operating expense is very low, mostly comprising a small office force and a small amount of space. It is to be remembered that brokers, as such, never come into possession of the goods which they sell, and do not need facilities for handling them. The percentage which they claim is distinctly a payment for service. In the case of jobbers, the expenses are much larger, although usually they, like brokers, charge a definite percentage. These middlemen, like the retailer, must calculate carefully the items of expense, so that they may adequately determine the necessary increase in price.

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[5] Hess, *Productive Advertising*, p. 183.

**267. Who Pays for Advertising?**—A question that has been widely discussed, both by economists and by business men, is who pays the advertising bills? This query is not of fundamental importance, because the effectiveness of advertising has long since been demonstrated. It may be well, however, to see definitely what lies behind the question.

It is clear in the first place that the bill for advertising is sent to the advertiser. For the moment, therefore, he pays the expenses. This advertiser, however, may charge the amount which he has spent for his advertising campaign either as an investment or as an expense. In any case, his policy will be to get the money back with interest. Whether he accomplishes his purpose or not, it is obvious that he expects to make the advertising expense a part of the price of his goods. This holds true whether the advertiser is manufacturer, jobber, or retailer.

The advertiser may secure repayment either by accumulating a return from more units of goods sold or from a lowered production or handling cost per unit or from both. The general principle, therefore, is that the man who spends money for advertising tries to shift that expense by (1) getting more people to spend their money for his goods; (2) getting people to spend more money for his goods; (3) by a combination of the first two ways.

If the advertiser fails in his advertising campaign, that is, if he is not able to accomplish either one of the aims stated above, his business must stand the expense. On the other hand, if he is successful, that is, if more people buy, they do so either by substituting these advertised goods for other goods, or by spending more of their earnings. Furthermore, if they substitute advertised goods for others, some manufacturer, jobber, or merchant loses a part of his trade. On these conditions, he would lose what the advertiser makes. If people spend more money as a result of advertising, they pay either from increased purchasing power or by saving less.

A further consideration in this connection is that every dealer in advertised goods will so price those goods as to return him all cost, including advertising bills, plus a profit. In other words, every price of every advertised product under normal conditions has as one of its elements advertising expense. It may be true, however, that in particular cases the advertiser may be able by increased volume of business actually to lower the price which he charges. The essential question is still unanswered.

It is estimated that more than $1,000,000,000 are spent annually in advertising campaigns. Is this amount an expenditure for real service? Is it merely for the buyer's privilege of purchasing a certain brand of goods at a price which includes the expense of advertising, or of buying a certain dealer's goods instead of those handled by another at the same price, or of buying advertised goods at a less price than would be necessary to charge without advertising? In other words, would the cost of distribution be greater or less if the $1,000,000,000 were not paid? That A takes B's trade away from him is not absolute proof of greater service or of greater efficiency. That the public now buys package and canned goods at a considerably higher price than is charged for goods in bulk is not absolute proof of greater service or greater efficiency.

It has been said in defense of advertising that this expenditure is an investment in goodwill. The character and quality of certain goods are by means of advertising associated with the maker of the products, or the merchant who sells them. This defense is not wholly satisfactory. Should the customer be charged for goodwill? Is not this the old question of paying for honesty? In modern business, is not honesty that must be paid for too dear at any price?

It is from such considerations as these that economists have said the advertising expense is a social waste. The contest between merchants and manufacturers to secure buyers when these manufacturers and merchants offer practically the same character and quality of goods means a duplication of effort; hence a waste of social energy. It is also pointed out that the standardization and identification of goods may have the effect of toning up quality and of simplifying the process of distribution of these goods.

A further consideration is that advertising service is a great directive force in modern business. If it is carried on with honesty and intelligence, the purchasing power of the consumer will be directed more wisely than if advertising did not exist. Clearly advertising is an appeal to the consumer, and with the tremendous expenditure in these modern days, it is no doubt a large factor in directing the purchases which he makes. There is further a grave responsibility on the advertiser to deal fairly and honestly with the consumer in carrying on his advertising.

**268. Buying Advertising Space.**—It was originally the duty of the advertising agency to be a broker of advertising space. It acted as an intermediary between the financial manager of the newspaper or magazine and the manufacturer or merchant who had goods to sell. As the power of advertising became more and more clearly recognized, the amount of space in the various media was greatly increased. To-day it is generally conceded that the returns from advertising are essential for the financial success of all newspapers and magazines. The charge for advertising space in these media is a charge for service which they perform. This service of publicity is determined by several factors. The first of importance is the amount of circulation. Of almost equal importance is the character of the reading public which it reaches. The character of the periodical itself, the number of advertisements which it carries, the time of day when it appears, or the time of month, are all considerations. Analogous factors enter into the charge for other media, such as billboards, streetcar cards, etc. Practically the charge for space is also modified by the character of the insertion. One periodical divides the modifying factors in its charges into position, display in fixed space, display on open contract, reading notices, and classified advertisements.

The buying of space in advertising media is a problem which requires special study. The point to be noted in this connection, however, is that the most important charge in advertising expense is the buying of space.

**269. Price Influences.**—Upon the problem of determining the price that shall be set by the manufacturer upon goods which he has made, by the jobber upon the goods which he handles, and by the merchant in retail trade on his stock is concentrated the best judgment of the business world. The price to be asked is set after all factors have been carefully considered. It is in fact the culmination of a process of careful analysis. If it is done with intelligence, there will be behind it a comprehensive analysis of the commodity, its market, and all of the essential costs. Some of the important considerations which enter into the setting of price are examined here.

The chief consideration is the relation of raw materials to the price of manufactured goods. In some instances, the relationship is not of great importance. In other cases, the price of raw materials is practically the dominating factor. It is often the case that the price of raw materials will fluctuate far more than the price of the products made from them. This is true, for instance, of crude petroleum and its products. Experience during the period of the war demonstrated the fact that the crude petroleum prices ran immediately in sympathy with the existing condition of production. The violent fluctuations that occurred in the prices of crude petroleum were not to be found in the prices of petroleum products.[6]

In the case of the prices of tobacco and tobacco products, experience during the last few years has shown that the raw material price rose considerably, quite a long time before the price of the finished products. "Prices of finished tobacco products did not begin to rise in earnest until the last half of 1917, three years after the outbreak of the war, and two years after the beginning of the general rise in prices. On the whole, their rise lagged behind the rise of prices of tobacco leaf."[7]

In this case, the price of the finished product began to increase about the middle of 1917. The reason given for the slowness in response to raw material prices is the fear of injuring the market for well-known brands.

Tobacco products have long been marketed to the consumer on the basis of brands at a price in a convenient number of cents (as a five-cent cigar, five-cent package, etc.), so that the brand and price became closely associated in the mind of the consumer. It was only after an extensive advertising campaign on the necessity of increasing the price that an attempt to raise it was made. It was largely this factor of the marketing situation which prompted postponement of the rise in price of the finished product, while at the same time the factor of relatively cheap raw materials made it possible to do so without loss to the manufacturer.[8]

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[6] War Industries Board, Price Bulletin No. 36, "Prices of Petroleum and its Products," pp. 49-54.

[7] War Industries Board, Price Bulletin No. 19, p. 8.

Even in the case of allied goods, such as that found in building materials, the relation between the price of raw materials and the finished product is frequently quite diverse. The study made by the Government into the prices of building materials shows that the increase in prices of finished products did not come at the same time or for the same reason. The price of stone, for instance, was advanced, in some cases, in direct conformity with the rising cost of production and without regard to the rapid decline in the demand for building material. In the case of marble, limestone, and granite, the prices were not raised to correspond to raw material prices. In the case of paint, the price rose to a higher point than that of any other building material with the exception of steel, due directly to the increased price of materials and especially of linseed oil. The price of nails, also, advanced more rapidly than that of almost all other building materials because of the demand for steel.[9]

There are often artificial influences which interfere with the correspondence of raw material prices to the prices of finished products. This condition was illustrated during the war by the rapid changes in the prices of certain manufactured goods. In the case of buttons made from ocean-pearl shells, there was a steady decline in price from 1913 to 1917, with but a slight recovery the following year. The reason for this was the closing by blockade of the principal European markets, and the submarine dangers. In this instance, the price of raw materials fell while the price of manufactured commodities rose sharply.

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[8] *Ibid.*

[9] War Industries Board, Price Bulletin No. 6, p. 12.

The relation between the price of raw cotton and cotton materials remained a direct one throughout the period of the war. There is, however, one peculiarity even in this instance. While the price of intermediate and finished cotton products moved in direct accord with the price of raw cotton, the margin of increase of cotton fabrics was much greater than that of yarns, and the margin of increase in the price of yarns was greater than that of raw cotton. The explanation in this case is that the demand for finished fabric was very urgent, that is, the goods must be had at once and at any cost. There is, no doubt, another element in the fact that manufacturing costs were greatly increased during the period. Throughout there was a speculative element.

In the case of silk goods, the price in the United States is determined directly by the trend of price in the Yokahama market. This is due to the fact that the United States depends directly upon Japan for raw silk. It has been found, nevertheless, that during the period of the war, price fluctuations for different kinds of raw silk were not identical. This divergence was due to differences in grading, in uses, and to local conditions. "Nevertheless, the Yokahama market sets the pace."[10]

The finished goods may be by-products of manufacture. This is illustrated in the case of leather. The hides from which leather is made are a by-product of the packing house, where animals are killed primarily for their meat and not for their hides, from which the material for leather is obtained. The cost of production, therefore, becomes a minor consideration. In attempting to determine a fair price for leather during the period of the war, it was found that an allowance of 13½ cents for tanning would make the tanner a profit of 10 per cent annually. A peculiarity in this case was that no consideration could be given to the subject of turnover. It was claimed by the tanners that there was only a single turnover during each year.

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[10] War Industries Board, Price Bulletin No. 25, p. 7.

Another influence in the determination of price is the element of style. In attempting to fix the price of hides the War Industries Board discovered that "Not a small factor in causing the greater advance in glazed kid leather and in women's shoes was the style then in vogue which ran both to extreme height and to many colors. This style caused a demand both for a large number of shoes and for larger quantities of leather to be used in each pair of shoes, besides the inevitable loss and waste due to the changing styles, and the advance of price to guard against this contingency."[11]

Such factors as this tend to produce high prices both of leather and of shoes. There is in all style goods an element of speculation. Style is largely a matter of taste and whim and caprice on the part of the consumer. In the case of piece goods for women's clothing it has been said that

> just what determines the selling properties of a design remains a mystery to the dress-goods designer. Two designs may be identical except for some trifling difference in structure; one may be a good seller, while the other fails to move at all. A design which has started being a good seller may give way in mid-season to a pattern which had shown no life at all in the early part of the year. This risk of failure to sell in the case of finished products cannot be reduced to anything like a safe or economical minimum. The successful fabrics, therefore, are obliged to carry the cost of the failures.[12]

Price in the United States has recently been greatly affected by governmental influence. This influence has been exerted in two different ways. In the first place, there has been a direct control of the price that is to be asked, which was either an absolute setting of price or a fixing of the percentage of profit. In the second place, the government owned enough stocks to regulate the price in the market. The effect of government-owned stocks in the determination of the price of wheat is well known. The same kind of effect has occurred in the case of wool prices and the prices of wool products. Because the price of wool was so greatly dominated by the government, it was not possible for the manufacturers of wool products to estimate in advance how much they were likely to pay for raw materials. Because of this uncertainty, a wide margin of safety was demanded in the price of woolen cloth.

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[11] War Industries Board, Price Bulletin No. 26, p. 10.

[12] Cherington, *Wool Industry*, p. 179.

Another element affecting price levels in connection with government activity is the tariff. On the theory that small industries should be protected against powerful foreign competitors, an artificial barrier is set up in the way of a tariff wall, and the consumer is compelled to pay an added price on account of the weakness and inefficiency of the domestic manufacturer. In so far as this is the case, there will be a higher price for finished goods in the market. It is obvious that if the domestic manufacturer cannot meet his foreign competitor on equal terms and, through competition in his own market, is compelled to hold his prices at a low level, there will be no additional burden on the consumer. Experience in the United States, however, has shown that a high tariff tends to create high prices.

Another consideration of much importance is the weather. An unusual season will have a substantial influence upon the prices of certain commodities. This influence, of course, affects the prices indirectly through demand or supply. A late, cold spring may greatly reduce the demand for spring goods. It may likewise affect the market for farm machinery. In the larger cities, the bakers adjust their daily supply, in part at least, to the changing weather conditions. This necessarily is a local factor and is one of the general risks of business.

Beyond these more or less tangible factors affecting the price of finished products, there lies a field of psychological influences which are not easily traced. The great disturbance throughout the world in recent years has so disorganized business, has so greatly affected both demand and supply, that business men, and the consumer in particular, have lost their bearings. In more normal times, the consumer was accustomed to demand a definite explanation for increase in price. Recently, however, so much has been written about changes in supply of materials that he has been trained to expect repeated increases and has come to accept them often without question. It frequently happens that in the stock and produce exchanges the buyers and sellers are thrown into a panic and prices fluctuate with great rapidity and without definite reason.

**270. Price Systems.**—As has been said, prices tend quickly to settle into a more or less definite system. This is particularly true of the retail price. Wholesale prices, in general, are more sensitive to changes and fluctuate more rapidly and more violently than the retail price. The theory of free competition holds that the market will determine fair prices which will always be in close relation to the costs of production. The foundation, therefore, of every price system, whether wholesale or retail, is the cost of production. Below this no price can ever go for a long period of time. Above this there is a fair field for competitive effort. In case of keen competition, the general belief has been that prices will settle close to costs of production, so that a stable system will be developed.

If at any time, however, there is a "run-away" market, due either to a violent change in production or in consumption, the system tends to break up. When such influences reach the retail market, they usually come with accumulated violence. Through such a period the world is passing at the present time. Until conditions both in the field of production and in the field of distribution have become sufficiently stabilized so that prices can become reasonably regular, it will not be possible for the world to return to normal conditions. In other words, the so-called normal condition of business is a stabilized market based upon a wholesale and retail price system.

**271. Profits.**—The aim of all business activity is to realize a profit. Practically speaking profits appear as two different kinds. One is the gross profit which contains the elements of expense, and the other is the net profit which is considered to be the return to management. Naturally the gross profit is much larger than the net profit. It has been estimated that the net profit in retail business throughout the United States has averaged 5 or 6 per cent on the capital invested. This margin, however, between costs and returns marks either efficiency of management or the capitalization of unusual profits.

It is the opportunity for making a profit that is the great directing force in business to-day. It must be remembered that men do what pays them best or at least what they think will pay best. The number of manufacturers, of jobbers, and of retailers will largely be determined by their expectation of profits. The kind of industry in which the manufacturer will engage, the kind of goods which the jobber and retailer will handle, will likewise very largely be determined by the profit opportunity.

The price asked for commodities is one which is set for the purpose of realizing a profit. The goods made by the manufacturer and handled by the jobber and retailer must sell. In all merchandising, the most important factor is the number of times the stock of goods is "turned." Profit is realized on units of commodities. But the percentage of profit is determined by the amount of capital invested. Small capital, with rapid turnover of goods, is the best means of securing merchandising success. The volume of business done is no basis for judgment until the amount of capital needed and the number of times the stock of goods has been sold out are determined.

**272. One-Price Policy.**—One striking difference between methods of retailing in the United States and those abroad is the so-called "one-price policy." This policy has had a rapid development in this country and has been found so acceptable to the consumer that most retailers have been compelled to conform. It consists in offering goods at a definite, announced price at which any consumer may purchase and below which the retailer refuses to go. Retail stores, however, that maintain a one-price policy have found it necessary to hold special or bargain sales in order to quicken the flow of goods from their shelves.

**273. List Price.**—One method of announcing the price of commodities by manufacturers and jobbers is somewhat inconsistent with the one-price policy of the retailer. This is known as the list-price system. An announcement is sent to the retailer by the manufacturer or the jobber stating that certain goods may be purchased and that the list price is so much. In order to stimulate cash payment and to reduce the credit risks it is further announced that from this list price there will be deducted for instance 60 per cent, 5 per cent, and 2 per cent for cash payment. These stipulated reductions are usually a part of the list-price system. Special, or inside, prices are sometimes given in connection with list prices.

**274. Discounts.**—An important point to be considered in connection with all prices of manufactured goods is the possible discount which may be obtained by prompt payment. The credit problem is always a difficult one and one filled with great risks. In order to reduce it, the dealer, manufacturer, or jobber may offer certain percentages of discount for cash. Discounts, however, may be granted for other causes. There are, for instance, quantity discounts, and there are discounts for the purpose of securing goodwill from those who buy continuously and in considerable quantities. No discount can be given, of course, without some return. Charges are constantly running against goods from the moment they enter the manufacturing process until they reach the consumer. A pertinent query to all offers of discounts is, what return does the giver of discount receive for it?

**275. Seasonal Prices.**—There are variations in the prices of merchandise due to seasonal demand. In most commodities, for example, the price level rises from early autumn to the beginning of the holiday season at Christmas. Then follows a sharp fall in prices, so that January generally marks a distinctly low ebb. There are also the spring prices and the fall prices, and there are the special summer prices for the purpose of stimulating business in dull seasons. Just as many commodities have a fluctuating supply, so they have a fluctuating demand. There will be found a constant tendency for the price level to move in conformity with these fluctuations.

**276. Speculative Prices.**—In the roundabout process of to-day there is much buying ahead of time and a consequent speculative element in business. Future buying may be done in either of two ways: there may be a price definitely agreed upon, in which case the seller takes the speculative risk; or the sale may be made with the condition that the buyer will pay the market price at the time of delivery. In this case, the buyer takes the risk. In all circumstances, however, there is this speculative element and there is a price margin of safety in future buying.

**277. Transportation Charges.**—Generally speaking the transportation charge on manufactured commodities is not of special importance. So many of these goods move in large quantities and are sold on the basis of so small a unit, that the actual charge for transporting to be allocated to each unit is practically unimportant. The United States, however, is a large country and the transcontinental rates usually find some reflection in prices. Many public announcements, therefore, contain a stipulated price for the commodity, adding a special price for the "Far West" or "West of the Rocky Mountains." It sometimes happens that this addition to price amounts to 50 per cent.

## SUGGESTIONS FOR STUDY

The following topics will be found useful by the student in his study in connection with the foregoing chapter:

### *General*

1. The annual advertising expenditure.
2. The consumer and the advertising bill.
3. Non-advertisers and the advertising expenditure.
4. Production costs and advertising.
5. Distribution costs and advertising.
6. Prices and advertising costs.
7. "There's a charge for store rent and a charge for advertising in the price you pay for every pair of shoes."
8. "We have invested approximately $1,000,000 in advertising and missionary work to get the proper distribution, but not a cent of that was ever charged to the goods themselves."
9. "And indeed it is only fair that this cost should be borne, in the last analysis, by the advertiser, for he is primarily responsible."

### *How Much to Spend for Advertising*

1. Percentage and lump-sum appropriations.
2. Advertising as an investment in goodwill.
3. The appropriation problem of a "going concern."

4. The appropriation problem of a new concern.
5. High advertising expenses and credits.
6. The appropriation as related to the kind of business.
7. The problem of distributing the appropriation.
8. The amount to be spent as affected by the purpose in view.

### *Advertising Costs*

1. Space cost data for (*a*) magazines, (*b*) newspapers, (*c*) trade and technical journals, (*d*) outdoor advertising, (*e*) street-car advertising.
2. Agency charges.
3. Cost for advertising "service."
4. Standardizing advertising costs.
5. The costs of guesswork.

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# CHAPTER XXII

## MERCHANDISING AND SOCIAL CONTROL

**278. The Forces of Social Control.**—The consumer has several kinds of defense in the bargaining process. His will must give consent, generally speaking; it is in his power to buy or to refuse to buy. He cannot purchase beyond his ability to pay; his purchasing power is limited. Both of these are individual considerations. Society, or consumers as a group, defend themselves by various kinds of social control; they enact laws, and these are enforced by the police power and interpreted by the courts. They develop customs; they control commercial activity by concerted action. In a broad sense, the "consumer is king."

Business is carried on under the direction of social control. Law has been defined as the crystallization of the public will. However imperfectly that will is registered, it is clear that commercial law is the result of an attempt to establish principles of abstract justice in business dealings that receive the sanction of the collective judgment of men. A sale, for instance, is a contract, and the terms of the contract are enforced by the collective will of the people. As business has increased in complexity, the consumer's individual ability to bargain on an equal basis with the merchant has grown relatively weaker. The effort to restore the desired equality is manifested in laws and regulations.

As has been pointed out so convincingly in that epoch-making book by the late W. G. Sumner, *Folkways*, there were in primitive society two great regulative forces, one positive, the other negative. Tradition determined what was the right thing to do; "taboos" determined what was not to be done. In modern society, also, there are two forces at work for social control, the ethical and the political. The former arises from sentiment, the latter from careful consideration and deliberate device. Both of these affect human conduct, in business as elsewhere. Instances of both kinds of control will be considered briefly for the purpose of showing that trade operates freely only under the rules established by social control.

**279. Enforced Competition.**—The will of the people has registered itself in laws to compel business men to compete with one another. One instance of such law is found in the Interstate Commerce Act of 1887, and another is the Sherman Anti-Trust Law of 1890. It is unlawful for business men to combine in restraint of trade. In general, business must be carried on under enforced competition. This applies to merchants as well as to manufacturers.

Modifications, however, have been made to this sweeping regulation. By the Clayton Act of 1914, workmen and farmers were exempted from its provisions. Concerted action by these two groups is not unlawful. A further modification has been made by the interpretation of the law by the Supreme Court in the cases of the American Tobacco Company and others, where the "rule of reason" has been applied. Further limitations were placed upon the application of the law by the passage in April, 1918, of the Webb Bill, which makes it legal to combine for export trade.

These enactments show clearly that the popular mind changes from time to time on such complex problems as competition offers. Nevertheless, the individual business man must obey the popular will as it finds expression. The entire concept of this subject is to-day doubtless undergoing a change, more or less radical, and the business policies wisely and farsightedly directed will mark these changes and adjust themselves accordingly.

**280. Protecting Standards.**—One way in which business makes progress is by raising the standards of quality. Not only must goods be what they are declared to be, but they must not contain adulterants. The will of the people declared this in the Pure Food and Drug Act of 1906. The foisting of patent medicines with unknown content upon an ignorant public is no longer permitted. The contents must be clearly and conspicuously printed on the bottle or package. Under stress of war some commodities have deteriorated, and there will be needed a painful struggle to regain lost ground. But it will be done, and progress will continue.

With the advent of package goods, where inspection is no longer possible, the need for further protection of standards is felt. The deviation from standard may be either in quantity or in quality. Net weight of contents must be stated, and the merchant is penalized for any kind of falsification. There is a similar control over quality. Business ethics of to-day demands that business men shall practice the "all-wool-and-a-yard-wide" principle.

It is obvious that long-range business requires the enforcement of standards. A few dishonest men, against whom there is no protection, would be able to demoralize business. The will of society has therefore declared that what the majority desire shall be the rule for all. Breaking away from standards in order to deceive is "taboo."

The principle holds for measure as well as for weight and quality. False bottoms in containers are illegal. It is still permissible, and all too frequently practiced, to construct a deceptive container; it is made to look larger than it really is. Thus bottles have hollow bottoms and boxes have edges extending beyond the bottoms. Business men who practice these deceptions are obeying the letter of the law only. In time they will not be allowed such petty deceits.

**281. Protecting Rights.**—Society, through the enactment of laws, protects individual rights. This fact is illustrated in all forms of property rights of individuals and corporations. It enters also into all kinds of trade relationships, not only by enforcing contracts of sale but also in protecting patent rights, copyrights, and goodwill.

The very definition of a patent shows the motive behind the social control of patent rights. A patent right gives to the owner the exclusive privilege of making, using, and vending any new and useful art, machine, manufacture, or composition of matter. It is society's method of encouraging inventive genius; it guarantees to the inventor the sole right to the results of his ability, in so far as he can make it effective. Patents, along with all of their rights, can be bought and sold in the market, but these rights are vested in the inventor until he willingly gives them up. And for a further assurance that society itself may benefit by the invention, the law sets a limit to the length of time that a patent can run.

Similarly, a copyright gives exclusive right to multiply copies of a published intellectual work. This right is readily secured by the author or publisher by the payment of a nominal fee of one dollar and by depositing two copies in the Congressional Library. In this way society seeks the general benefit of intellectual ability.

As affecting trade more directly there are the protective rights pertaining to trade-marks. While patent rights and copyrights are statutory, trade-mark rights are those of common law. The one essential for acquiring these rights is "priority of adoption, coupled with actual use upon goods in the market." The goods to which they are attached must be saleable and on sale in the market. "In general, any merchant, manufacturer, dealer, or any one who is a trader, or conducts a commercial establishment, hotel, newspaper, or magazine, may identify his product or business by any lawful mark and be protected against infringement.''[1]

In connection with the protective rights pertaining to trade-marks and trade names, there is the question of goodwill. The fundamental principle to which social will has been reduced is thus simply stated: ''No one has any right to sell his goods as the goods of another.'' Goodwill, protected in this way, is considered as a tangible, substantial thing, resulting from the offering by the business man of a distinctive mark, quality, or service. It is to encourage honorable and fair dealing, the handling of wares of the highest quality, and any form of service for the customer's complete satisfaction that society has laid down this simple principle.

**282. Enforcing Honesty.**—Because evil practice by a few may discredit the many, society has demanded laws to punish the dishonest ones. More and more, society is trying to enforce honesty upon every business man; honesty in dealings with the consumer and with other business men. This desire underlies the laws to regulate advertising.

There are, in general, three types of laws in force for protecting the public against dishonest advertising and false pretenses in merchandising. One is the so-called ''model statute,'' which is now a law in eight or more states, and reads as follows:

> Any person, firm, corporation, or association who, with intent to sell or in any way dispose of merchandise, securities, service, or anything offered by such person, firm, corporation, or association, directly or indirectly, to the public for sale or distribu-

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[1] E. S. Rogers, *Outline of Law of Trade-Marks.*

tion, or with intent to increase the consumption thereof, or to induce the public in any manner to enter into any obligations relating thereto, or to acquire title thereto, or an interest therein, makes, publishes, disseminates, circulates, or places before the public, or causes, directly or indirectly, to be made, published, disseminated, circulated, or placed before the public, in this State, in a newspaper or other publication, or in the form of a book, notice, handbill, poster, bill, circular, pamphlet, or letter, or in any other way, an advertisement of any sort regarding merchandise, securities, service, or anything so offered to the public, which advertisement contains any assertion, representation, or statement of fact which is untrue, deceptive, or misleading, shall be guilty of misdemeanor.

There is another law very similar to this, but amended by the insertion of the word "knowingly" or some such term, before "makes, publishes, disseminates, etc." This insertion definitely places the burden of proof on the prosecution. It must be demonstrated that the advertiser knew what was said was false and intended to deceive. To prove motive is never easy.

A third type of law, following the Massachusetts enactment, penalizes the advertiser for a false statement of fact about his merchandise. An Illinois Act "to prevent fraudulent advertising," approved June 19, 1915, runs thus, the italics being the author's:

SECTION 1. *Be it enacted, etc.,* that whosoever, being any person, firm, corporation or association, in a newspaper, periodical, circular, form, letter, or other publication, published, distributed, or circulated in this commonwealth in any advertisement in this commonwealth, *knowingly* makes or disseminates, or causes to be made or disseminated, any statement or assertion concerning the *quantity,* and the *quality,* the *value,* the *merit,* the *ability,* the *use,* the *present* or *former price,* the *cost,* the *reason for the price,* or the *motive or purpose of a sale,* of any *merchandise, securities, service,* or *anything of value;* or concerning the *method* or *cost of production* or *manufacture* of such *merchandise;* or the *possession of rewards, prizes,* or *distinctions* conferred on account of such merchandise, securities, services, or anything of value; or the *manner* or *source of purchase* of such merchandise or securities, or thing of value with intent to *sell* or in any wise dispose of such merchandise, securities, or thing of value; which is *untrue* or *calculated to mislead* and *know* to be so by said person at said time, shall be guilty of a misdemeanor, and on conviction be sentenced to pay a fine of not more than one thousand dollars, or by imprisonment, in the county jail not exceeding 60 days. or by both such fine and imprisonment.

**283. Price Control.**—In a time of emergency, when society itself is in danger, private interest must yield to public interest. This fact was demonstrated during the world war, in the United States as well as elsewhere. Among other ways it found expression in price regulation and control. Beginning in August, 1917, the government price control extended to the signing of the armistice in November, 1918. Although control at this latter period was greatly relaxed, there was still regulation affecting trade, as in sugar, wheat, and flour.

Necessity from a social point of view dictated the extension of governmental power over prices. From 1896 on there had been a continued rise in price level. The high cost of living was a common topic of discussion before 1914. With the opening of the war, there were new increases and more widespread unrest. After the United States entered the war there was another rapid rise. The cry of profiteering was begun. Some curb on private greed was demanded. The answer to this demand was governmental control.

It was a new venture for our government, and therefore no precedent had been set. Knowledge of even the fundamental facts was lacking. In consequence, many mistakes were made. In some cases the price of the finished product was fixed, but not the price of raw materials.

Other instances showed miscalculations. Yet, crude as the methods were and mistaken as the judgment was, the entire experiment illustrates the use of social control in business.

**284. Public** Utilities.—The recognition of social control behind business activities is further demonstrated in the case of public utilities. These enterprises have been defined as "private property devoted to public service." They comprise those types of business which have been declared of so much concern to society as a whole, so intimately connected with general welfare, that everything that affects them is of public interest. As a result, railroads, street railways, water plants, gas, electric light, warehouses, pipelines, have been set apart from all other business and required to operate under special regulation and supervision. Banks may be called semi-public businesses; and likewise insurance companies. These, too, have special regulations.

There is no clear line of division between public utilities and many businesses of vital importance to the public. The tendency appears to be, at present, to extend the list. Carried to an extremity this movement arrives at a socialization of industry. Of this type of social control, coöperative enterprises are illustrative. Collective management by a group is the direct operation of social control.

**285. Methods of Control.**—There are numerous methods by means of which social control may declare itself. Some of these are organized methods; many are not. Public interest manifests itself often in unexpected ways. Several of the most important ones are suggested below.

**286.** *1. By Enacting Laws.*—Through the various political organizations the social will may declare itself. Federal, state, and municipal laws prohibit directly certain business activities. Liquor and opium traffic has thus been prohibited. Such laws may not only prohibit, but may also command or permit the doing of certain things in a certain way. Under all of them, prohibitive, mandatory, or permissive business must operate.

**287.** *2. By Licenses or Examinations.*—Individuals may be prevented from engaging in business and the business itself may not be permitted to operate unless certain licenses have been issued. All professions require examination of those who would enter. Licenses must be held by druggists, barbers, engineers, chauffeurs, and others. It has even been suggested that retailers of all types should be required to hold licenses. The requirement of examinations and licenses is society's method of defending itself against ignorance and incompetence. If this method is recognized to be working poorly, other and more effective means will be devised. It is the social will that business be done more and more efficiently.

**288.** *3. By Taxation.*—Governmental power of taxation is sometimes invoked to control business activity. In part this may be a method of discouragement, by handicapping the individual or his business. Or the burden of taxation may be made so heavy as to act as a positive prohibition from engaging in a particular business.

This method is well illustrated in the case of trading-stamp companies. There are several states that have imposed such heavy taxes, not only on the companies issuing the stamps or coupons but also upon every retailer who uses them, as to make it impossible to carry on the business. In the State of Washington, for example, there is a law that imposes a license tax of $6,000 annually upon every company that sells stamps to retailers and upon each merchant who uses them. In Florida, there is a law requiring the payment of an annual tax of $500 to the state and another of $250 in each county where business is done. Obviously, the purpose of such taxation is to prohibit, not to regulate.

289. *4. By Force of Example.*—A type of unorganized control that finds expression by force of example is illustrated by the introduction into retail business of the one-price policy. Credit for introducing this policy is given to John Wanamaker, when he began his retail experience in Philadelphia. Whether or not this is historically true, he has consistently practiced it. Other leading merchants adopted the policy also, and the consuming public was pleased with it. So effective did the policy prove that the majority of retail merchants were forced into line, and today the old-fashioned, crude higgling over prices is no longer considered good business practice. This is the ancient principle of a little leaven affecting the whole lump. It shows, too, that the popular endorsement of an example is a powerful means for control. A single individual or a small group may stand as the public's expression of a standard to which all others must measure up.

Another example of the working of this principle is found in the adoption of a standard closing time. In many instances, to be sure, a municipal ordinance embodies the popular will. But in a multitude of other cases, the opening and closing hours are "adopted by common consent." This illustrates the unorganized force of example.

A different phase of this same power of control is to be found in the censorship of advertisements. There are certain magazines, for example, that refuse copy which does not meet their standards of business ethics. This policy, also, has received popular approval, so that the columns of those periodicals have unusual advertising power. Business men are glad to trim their policies in order to secure entrance into these advertising media. Herein lies a power for control.

290. *5. By Group Action.*—Social control may be exerted through group action among business men themselves. Examples of this fact are found in trade associa-

tions. Members of these associations are made to feel the disfavor of their fellows when their practices are below standard. The effect is a powerful one. Control in such organizations may go so far as to find expression in various kinds of discipline.

A specific instance of this method of control is to be found in the Associated Advertising Clubs, where a vigilance committee was organized for the purpose of improving advertising practice. Cases of bad practice were watched for, and the business men who were guilty of such were interviewed, and even prosecuted, if the practices were illegal and were persistently carried out.

**291.** *6. By Publicity.*—As sunlight is fatal to many undesirable germs, so the light of public knowledge is destructive to bad business practices. What men will do in secret is often far different from what they will do in the open. Open transactions openly arrived at are as much to be desired in home trade as in international diplomacy. It is for these reasons that publicity is a powerful force in directing and controlling business policies. Thus, published annual statements are required of many business concerns. Newspapers, too, must publish the facts about ownership and management of their columns, and furnish accurate data on circulation.

Because the public may suspect those methods that are kept secret, many managers have learned to take advantage of this desired publicity. There are manufacturers and merchants who make a business of keeping "open house." They advertise the fact that they have nothing to conceal. Stock exchanges often take great pains to make clear to the layman those peculiar methods which they employ. But too much business is still done secretively. Still, more and more the open door policy is gaining ground. Publicity will become a greater and greater power in toning up business practice.

**292.** *7. By Limiting Profits.*—Business is oftentimes badly shaken by sudden droughts, blights, storms, and other disasters. While trade is thus off center, some men may find themselves in strategic positions where it is possible to take advantage of other business men and of the public.

The social will does not permit an extortionate interest rate for money loaned. Occasionally, too, the profits allowed are definitely controlled. Men conduct business to make money, but society will not permit unbridled greed. This is called "profiteering," and is socially condemned. If the public disapproval is not enough to stop the practice, laws will be demanded to regulate and control the net returns.

**293.** *8. By Boycotting.*—Another powerful force to control trade rests with the consumers. They can refuse to buy certain commodities or decide to buy only in small quantities. During the war, there were meatless days, heatless days, gasoline-less days. There was refusal to buy extra clothing or luxuries. In the period of high prices following the war, there came into existence old-clothes clubs, overall clubs, anti-luxury clubs, and so on. The Canners' Association at a convention passed resolutions to boycott the sugar dealers.

Although the consumers are unorganized and make often abortive efforts to accomplish their desired results, their influence on the whole is fairly effective. "The consumer is king."

**294.** *9. By "Suggesting" Prices.*—In connection with the power of publicity, there should be considered the experience during the war of publishing a list of "fair prices" as a suggestion to dealers and consumers. This method had a powerful effect in determining prices. Coming as the suggestions usually did from an official body, even though that body had no authority to fix prices or to punish those who refused to regard the suggestions, they nevertheless smacked of official sanction.

Some powerful, private organizations have used this method in the past to control retail prices. Lists of suggested prices were given to the retail dealers, and the activities of these dealers were watched. If the suggested prices were disregarded, there were means at hand to discipline them.

**295. Machinery for Control.**—There are two types of machinery through which social control can function: governmental machinery and private machinery.

**296.** *1. Governmental Machinery.*—There are also two general kinds of governmental machinery: that devised for continued operation, and that created for emergency purposes. Of the continuous type there are the agencies described below.

The Interstate Commerce Commission was organized in 1887 to supervise railroad operation and establish maximum and minimum rates. The roads, at the time of its formation, were engaged in a rate war, and by means of cutthroat competition were destroying one another. Rebates and other unfair practices were rife. The commission is the public's representative to oversee the conduct of the transportation system.

The Federal Trade Commission came into being in 1914 for the purpose, primarily, of stopping methods of unfair competition. It was also intended by those who originated the idea that this Commission would become a great clearing house of trade information, and so be a powerful directive business force. Its activities, for the most part, have been investigatory, and the results of the investigations have largely been made public. Sometimes the Department of Justice has acted upon their recommendations and instituted proceedings against corporations.

There also was established a government body to supervise the foreign-trade interests of the American merchants and especially to develop a merchant marine. This is the United States Shipping Board. This board is granted power to own, operate, and control ships and to enter into competition with the domestic and the foreign shipping interests. Like the Federal Trade Commission, it can investigate and suggest changes in management and methods. Like the Interstate Commerce Commission, it can deal in an advisory way with freight rates. By means of its announced rates, it has been able to stabilize and, to a certain extent, settle the uncertainty of the rate schedules during the recent past.

Another government department having to do with the general control of business is the Department of Commerce. This Department especially through the Bureau of Foreign and Domestic Commerce, acts in an advisory capacity for business men who desire to develop foreign trade. It makes special investigations and it furnishes information of value to business men. Its power is, therefore, directive rather than one of control.

For the enforcement of law, the government has its Department of Justice. This Department in charge of the Attorney-General aims to enforce the laws that have been passed by the Federal Congress. It is, therefore, essentially a mechanism for control. In so far as its activities touch business relations, the social control is applied to business.

In addition to the continuous peace-time organizations described above, there have been organized several emergency boards for the purpose of directing and regulating business activity during the war. One of the most important of these boards from the point of view of the business man was the War Trade Board. This body had general charge of exports and imports and, through a system of licenses, controlled with a firm hand the character and amount of commodities to be brought into the country and to be shipped abroad. With the passing of the war, this Board went out of existence.

For dealing with domestic trade, there was created the War Industries Board. This body dealt with the problems of raw materials and manufactured goods, particularly in those cases where priority rights were necessary. The Board determined to what kind of industry materials should first be furnished, and suggested modifications in the manufacturing plans of non-essential goods. Like the War Trade Board, this organization went out of existence after the signing of the armistice.

Under the stress of the war, the railroads and the telephone and telegraph systems of the country passed under government control and operation. The Railroad Administration was put in charge of all the railroads and was directly responsible for their conduct. The Postmaster-General was in control of the telephone and telegraph systems. This illustrates the fact that when society is in danger, private interests are disregarded in favor of social interests.

Other bodies such as the Food Administration and the Fuel Administration were organized to defend the public against profiteering and to direct for the common interest these essential industries. Like the other emergency boards, they passed out of existence when the war was ended. As an after-effect of the war, there has come into existence such an organization for social control as the Massachusetts Commission on the Necessaries of Life. This body makes investigations into the cost of living and by publicity attempts to determine a fair method of carrying on business. The results of the investigations by this Commission, becoming known to the entire public, enable them to defend themselves against exorbitant charges. It is, however, only a temporary expediency.

**297.** *2. Private Machinery.*—In contrast with the government organizations are those that have been established by business men themselves. The most powerful of these are the trade associations. There are more than 3,000 of these associations in the United States to-day, and practically all are aggressively active.

They are usually based upon a community of interest, and are confined in membership to certain lines of industry or trade. There are numerous retail associations, jobbers' associations, and wholesalers' associations. There are credit men's associations, bankers' associations, and manufacturers' associations. All of these bodies afford an educational and a directive force in business. Through the discussion of common problems they often resolve on collective action to which the individual must conform.

So powerful have these agencies become in standardizing business methods and particularly in leveling out prices and reducing the field of competition, that there has come a reaction against them. It is felt by many that the trade associations accomplish the results which have been denied to combinations and monopolies by the law. If this complication occurs, there will be sooner or later restrictive legislation to reëstablish free and individual competition.

**298. Conclusion.**—The social control of business, therefore, is a strong directive force and has found expression in many different ways. If carried to extremes, the principle of social control will result inevitably in some kind of Soviet system. If the principle of socialization of industry which has been applied in many countries to essential industries is broadened in scope, there will be a further restriction of individual enterprise. It is only under a system of *laissez-faire* that the individual is comparatively free from restrictive social control. As business philosophy changes in regard to business principles, the controlling force naturally will change.

## SUGGESTIONS FOR STUDY

The student should now consider the elements of social control in marketing the commodity which he has under investigation. Classroom work may consist of discussion of the following topics:

1. Consumer defenses.
2. Economic aspects of social control.
3. Growing recognition of social control.
4. Social service aspects of merchandising.
5. Marketing problems under a socialistic régime.
6. Changing ethical requirements of business policies.
7. Business freedom under the law.
8. Historical development of business standards.
9. Experience with price control.
10. Government ownership and operation of business enterprise.

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